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17-1





No. 11116

W. 2434

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United States  
Circuit Court of Appeals  
For the Ninth Circuit.

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,  
Appellant,

vs.

C. H. FARRINGTON,  
Appellee.

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Transcript of Record

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Upon Appeal from the District Court of the United States  
for the District of Oregon

FILED

JAN 4 - 1946

PAUL P. O'BRIEN,  
CLERK





No. 11116

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Circuit Court of Appeals

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS  
OF RECORD:

SIDNEY TEISER,

W. G. KELLER,

738-749 Morgan Bldg.,

Portland, Oregon,

for Appellant.

CARL E. DAVIDSON

and STEPHEN E. PARKER,

1525 Yeon Bldg.,

Portland, Oregon,

for Appellee.



In the District Court of the United States for the  
District of Oregon

No. 2202

GEORGE M. McBRIDE, Trustee in Bankruptcy  
of WESTERN BOND AND MORTGAGE  
CO., an Oregon Corporation, Bankrupt,  
Plaintiff,

vs.

C. H. FARRINGTON,

Defendant.

### CIVIL ACTION COMPLAINT

George M. McBride, as Trustee in Bankruptcy of Western Bond and Mortgage Co., an Oregon corporation, by his attorneys, Sidney Teiser and W. G. Keller, complaining of C. H. Farrington, alleges:

#### I.

The action arises under Sec. 67 and Sec. 70 of the United States Bankruptcy Act as amended (U.S.C.A. Title 11, Sec. 107 and U.S.C.A. Title 11, Sec. 110.)

#### II.

On or about the 25th day of November, 1931, a petition of certain creditors of Western Bond and Mortgage Co., an Oregon corporation, was duly filed in the office of the Clerk of the United States District Court for the District of Oregon, and such proceedings were duly had thereunder that on or about the 24th day of September, 1934, the Western

Bond and Mortgage Co. was duly adjudged a bankrupt, and that thereafter, on or about the 4th day of December, 1934, the plaintiff, George M. McBride, was duly appointed the Trustee in Bankruptcy of said Western Bond and Mortgage Co. and thereafter duly qualified as such trustee and is now acting as such trustee.

### III.

That on or about the 20th day of December, 1930, the defendant, C. H. Farrington, was the president and a director of the Western Bond and Mortgage Co., and the beneficial owner of all, or substantially all, [1\*] of its outstanding common and controlling stock, such stock being held in his name and in the name of a corporation, all of the stock of which said defendant owned or controlled. That at said time said defendant, in full domination and control of said company, fraudulently and with intent to defraud said company, its preferred stockholders, its bond holders, and its creditors, and for the purpose of benefitting himself, transferred to another the controlling common stock in said company, and obtained through manipulation of the Western Bond and Mortgage Co. certain property of said company, viz., all the stock of the Western Guaranty Co., of the value of \$322,014.35, without the said Western Bond and Mortgage Co. retaining anything of value for its said property.

That the method and process of said transfer and manipulation was as follows:

---

\*Page numbering appearing at foot of page of original certified Transcript of Record

1. On or about the first day of December, 1930, while president and director of the Western Bond and Mortgage Co., and while in control of said company by ownership of substantially all of its common and controlling stock, said defendant, on behalf of the Western Bond and Mortgage Co., caused to be organized an Oregon corporation under the name of the Western Guaranty Co., with an authorized capital stock of \$5,000.00 par value, of which company he became president and director, and of which he had full dominance and control.

2. On December 15, 1930, without any resolution of the stockholders or directors of the Western Bond and Mortgage Co., and without any action of its board of directors, and without other authorization, defendant caused the Western Bond and Mortgage Co. to subscribe for all of the stock of the Western Guaranty Co. and in purported payment of the stock so subscribed for, transferred to said Western Guaranty Co. assets of said Western Bond and Mortgage Co. amounting to \$322,014.35 in value.

3. On December 20, 1930, at a directors' meeting of said Western Bond and Mortgage Co., of which he had up to that moment been president and director, and at which meeting he was present, the defendant permitted or caused the transfer to him, or to the Laurel Investment Co., (a [2] corporation which he wholly owned and controlled) all the said stock of the Western Guaranty Co., of the value of \$322,014.35, in purported consideration of certain securities which he had just re-

ceived from one who the moment before had succeeded him as the owner of the controlling common stock of the Western Bond and Mortgage Co., for the valueless stock in said Western Bond and Mortgage Co., which securities he held but for a moment, if at all.

4. That of the securities received by the defendant from the purchaser of the controlling common stock of the Western Bond and Mortgage Co. and immediately transferred to the Western Bond and Mortgage Co., the only securities having any value were some \$22,661.03 face value of automobile contracts receivable. Such contracts were then forthwith caused to be transferred by said Western Bond and Mortgage Co. to the holder of the newly acquired controlling common stock of said Western Bond and Mortgage Co. for other assets of no value.

That as a result of said fraudulent transfers and manipulations of the defendant just above set forth, the Western Bond and Mortgage Co. was caused to relinquish and dispose of assets of the value of \$322,014.35, for which it received and retained assets of no value, to the damage of said Western Bond and Mortgage Co. and of the plaintiff, of \$322,014.35, with interest on said sum at the rate of 6% per annum from the 20th day of December, 1930.

#### IV.

That on or about the 12th day of December, 1929, and for some time prior and subsequent thereto, the defendant, C. H. Farrington, was the president



and a director of the Western Bond and Mortgage Co., and the beneficial owner of all, or substantially all, of its outstanding stock, said stock being held in his name or the name of a corporation, all of the stock of which said defendant owned or controlled, and said defendant was in full domination and control of said company.

That at said time the Western Bond and Mortgage Co. owned and held 40,000 shares of the Consolidated Credit Corporation Class A no par [3] stock of the total value of \$120,000.00.

That at said time the Western Bond and Mortgage Co. held and was the beneficial owner of all of the stock of the Keystone Finance Co., said Keystone Finance Co. being a wholly owned subsidiary of the Western Bond and Mortgage Co.

That notwithstanding that the Western Bond and Mortgage Co. was the owner of all the stock of the Keystone Finance Co., on or about the 12th day of December, 1929, with the knowledge, consent, and at the direction of the defendant, the Western Bond and Mortgage Co., on or about said date, transferred out of the Western Bond and Mortgage Co., and to a person or persons unknown to the plaintiff, said 40,000 shares of Class A no par value stock of the Consolidated Credit Corporation of the value of \$120,000.00 in purported consideration of all the stock of said Keystone Finance Co., which said latter stock it already owned.

That said transfer was and is fraudulent and was fraudulently caused and permitted by the said

defendant, to the damage of the Western Bond and Mortgage Co. and of the plaintiff in the sum of \$120,000.00, with interest thereon at the rate of 6% per annum from the 12th day of December, 1929.

## V.

The actual fraudulent character of the transactions and transfers herein set forth was not discovered by the plaintiff until on or about the 21st day of September, 1943, and the probable fraudulent character of said transactions was not discovered until on or about the 27th day of July, 1943, at which latter time a report was made to plaintiff by a certified public accountant, who, upon authority of the Referee in Bankruptcy in charge of the Bankruptcy of Western Bond and Mortgage Co. was employed to make an examination of the books and records of the Western Bond and Mortgage Co. and the books and records of such affiliated companies as were in possession of, or available to, the trustee.

The true character of the transactions set forth in Paragraphs III and IV hereof were, by the defendant and those under his dominion and control, concealed and camouflaged by misleading and false entries on the books of the Western Bond and Mortgage Co., and were hidden and disguised by means of the [4] organization of dummy corporations to whom assets of the Western Bond and Mortgage Co. were transferred, or by whom liabilities were assumed, which entries and which jug-

gling of assets and liabilities were made and done, by and on behalf of defendant, for the purpose of keeping in ignorance and misleading those who might have the right to know the true character of said transactions. Said entries and said juggling did lull and mislead those whose right it was to know the truth, including the plaintiff.

On August 6, 1935, within one year from the adjudication of the Western Bond and Mortgage Company as a bankrupt, the United States of America filed an asserted priority claim of \$51,-451.11 for taxes additionally assessed against said Western Bond and Mortgage Co. That when said claim was filed for additional taxes, based on a revenue agent's report, the plaintiff, as trustee, searched the papers and records of the Western Bond and Mortgage Co. for such revenue agent's report, but no such report or any copy thereof was found in said papers. Plaintiff, as trustee, thereupon conferred with the Referee in charge of said estate for the purpose of obtaining an order upon the United States of America requiring the government to furnish him with a copy of such report, with the end in view of his contesting said claim of the government for taxes. At the time said claim was filed and continuously before and thereafter, until on or about the 11th day of February, 1943, the estate in bankruptcy of the Western Bond and Mortgage Co. had no funds to pay any claims over and above the cost of administration, and your trustee was thereupon instructed by the Referee in

charge of said estate that it was not necessary to make demand for or to require the production of said revenue agent's report, or to concern himself with the matter at said time, nor to make at said time any objection to the claim of the United States Government for taxes, since the allowance or disallowance of such claim would be the determination of a moot question unless funds came into the estate over and above that necessary to pay the cost of administration, and plaintiff was further directed by said Referee to withhold filing any objections to the claim of the Government until such time as the bankrupt estate might be in funds, if such time ever arrived. Accordingly, plaintiff, as trustee, made no investigation of the correctness of said claim for taxes, and made no [5] effort to obtain the revenue agent's report on which said claim was based. No funds came into said estate which could be applied to the payment of such claim until the 11th day of February, 1943, at which time a recovery was had in a suit instituted by plaintiff, as trustee, against one who had improperly received assets from the bankrupt estate.

Shortly after said funds came into the bankruptcy estate, plaintiff, as trustee, began an investigation of the United States Government's claim for taxes, for the purpose of determining whether or not objections should be filed to the claim asserted by the government for such taxes and, for the purpose of making such investigation, called upon the Collector of Internal Revenue of the United



States of America, at Portland, for a copy of the agent's report on which the United States Government's claim for taxes was based. All papers, including the agent's report, he was informed by the office of the Collector of Internal Revenue at Portland, had been sent to Washington, D. C., and that a copy of such report would be obtained for him as soon as practicable. Such report was obtained and a copy of it submitted to him by the said Collector of Internal Revenue at Portland during the first week in June, 1943.

Upon obtaining such report your trustee then made application to the Referee in Bankruptcy in charge of the estate of the Western Bond and Mortgage Co. for authority to employ a certified public accountant for the purpose of obtaining facts and data from the books and records of the bankrupt corporation, on which to base objections to the claim of the government for said taxes, and to prosecute such objections when made. Accordingly such authority was promptly granted to plaintiff, as trustee, and thereupon plaintiff employed the services of a competent certified public accountant to make such investigation. That the continuous work and services of said certified public accountant were required for a period of approximately two months before his report could be completed, and it was necessary for said certified public accountant, or any certified public accountant, to devote approximately that time in order to make the discoveries disclosed by such report. When

such discoveries were made and plaintiff informed thereof, certain other [6] factual data was necessary to be obtained in order to amplify the data supplied by said public accountant, the ascertainment of which required approximately a month of investigation by plaintiff and his attorneys.

Plaintiff nor his attorneys had any intimation or knowledge of the facts disclosed by the allegations of Paragraphs III and IV of this complaint, nor any knowledge which would put them on inquiry leading to such discovery, until plaintiff received the information contained in the said certified public accountant's report.

The estate in bankruptcy did not have sufficient funds until after the 11th day of February, 1943, with which to pay for the services of an accountant to make an investigation of the books and records of the Western Bond and Mortgage Company of the character and extent necessary to uncover the facts disclosed, even had any information come to plaintiff's knowledge leading him to suspect the fraud alleged herein.

Plaintiff has used due diligence to discover said fraud, but, notwithstanding said due diligence, and because of the cleverness of defendant in disguising and concealing the true character of the transactions, plaintiff did not discover the same until the time set forth above, and promptly after said discovery caused to be prepared this complaint, and said complaint was filed immediately after its preparation.

Wherefore, plaintiff demands judgment against the defendant, C. H. Farrington, for the sum of \$442,014.35, with interest at the rate of six per cent per annum on \$120,000.00 thereof from the 12th day of December, 1929 until paid, and with interest at the rate of six per cent per annum on \$322,014.35 from the 20th day of December, 1930, until paid.

TEISER & KELLER

/s/ SIDNEY TEISER

/s/ W. G. KELLER

Attorneys for Plaintiff

[Endorsed]: Filed October 2, 1943. [7]

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[Title of District Court and Cause.]

MOTION

Comes now defendant and moves the court for orders as follows:

(1) For an order dismissing the action on the ground

(a) That the complaint fails to state a claim upon which relief can be granted;

(b) It appears from the face of the complaint that this action is barred by the statute of limitations.

(c) It appears from the face of the complaint that plaintiff is barred by laches.

(2) For an order dismissing so much of the action as is embraced in Paragraph III thereof on the ground

(a) That said paragraph fails to state a claim upon which relief can be granted;

(b) It appears from the face of the complaint that the action on said claim is barred by the statute of limitations.

(c) It appears from the face of the complaint that plaintiff is barred by laches.

(3) For an order dismissing this action as to the claim set up in Paragraph IV of the complaint on the ground

(a) That said paragraph fails to state a claim upon [8] which relief can be granted;

(b) It appears from the face of the complaint that the action on said claim is barred by the statute of limitations.

(c) It appears from the face of the complaint that plaintiff is barred by laches.

If the foregoing motion be denied in whole or in part, or consideration thereof postponed, defendant moves the court for an order requiring plaintiff to make his complaint more definite and certain in this:

(a) That he allege what assets of Western Bond and Mortgage Co. he refers to in subparagraph 2 of Paragraph III which were transferred to West-



ern Guaranty Co. and the value of each of such assets at the time of said transfer.

(b) That he allege what securities, if any, he claims defendant traded for any property of Western Bond and Mortgage Co., setting up also the value of each item at the time of such trade;

(c) That he clarify the meaning of subparagraph 3 of Paragraph III which is now not understandable to defendant.

(d) That he allege whether he claims defendant was an officer or director of Western Bond and Mortgage Co. when said alleged trade was made.

(e) That he allege whether he claims defendant was an officer or director of Western Bond and Mortgage Co. at the time the automobile contracts referred to in subparagraph 4 of Paragraph III were transferred by Western Bond and Mortgage Co. and that he allege to whom said securities were transferred and for what consideration.

(f) That he allege what false entries in the books [9] are referred to in line 32 of page 4.

(g) That he allege what dummy corporations concealed the alleged transactions referred to in the complaint.

(h) That he set up what "juggling" hid any such transactions and what such juggling consisted of.

(i) That he allege the date the tax claim was first asserted against the bankrupt estate.

(j) That he furnish a bill of particulars setting up all of the book items upon which he intends to rely.

In presenting the motion to dismiss defendant will rely upon the proposition that it appears from the face of the first asserted claim that the trade alleged therein was consummated at a time when defendant was no longer an officer or director of Western Bond and Mortgage Co. and that he had a right to deal at arm length with said corporation, that the complaint fails to state any cause of action on account thereof and that the same is barred by the statute of limitations and laches.

As to the second claim it is not alleged that plaintiff took any Consolidated Corporation stock out of Western Bond and Mortgage Co. or in any way profited by any such alleged transaction or that it was other than the act of the corporation itself and that it affirmatively appears that the cause of action, if any, is barred by the statute of limitations and laches.

In presenting the motion to make definite and certain and for a bill of particulars, the defendant will rely upon the proposition that such information is necessary to enable defendant to prepare his pleadings and prepare for trial.

CARL E. DAVIDSON

JOHN F. REILLY

Attorneys for Defendant [10]

## NOTICE OF MOTION

To Teiser and Keller,  
738 Morgan Building,  
Portland, Oregon.  
Attorneys for Plaintiff.

Please take notice that the undersigned will bring the above motion on for hearing before this Court on the 8th day of November, 1943, at 10 A. M. or as soon thereafter as counsel can be heard.

JOHN F. REILLY

Of Attorneys for Defendant.

[Endorsed]: Filed Oct. 25, 1943. [11]

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[Title of District Court and Cause.]

ORDER UPON MOTION TO DISMISS AND  
UPON MOTION TO MAKE MORE DEFINITE AND CERTAIN AND ORDER FOR  
SEGREGATION OF ISSUES

This cause having come on this day to be heard upon Motion of the defendant to dismiss, and upon Motion to make the complaint more definite and certain, filed by the plaintiff herein, the defendant appearing by John F. Reilly, Esq., and plaintiff appearing by Sidney Teiser, Esq., and the matter having been argued and duly considered by the court;

It Is Ordered that said Motion to dismiss is hereby reserved for determination by the court

either at the time of pre-trial or at the time of trial, as the court deem proper; and

It Is Further Ordered that defendant be, and he hereby is, directed to answer the complaint herein; and

It Is Further Ordered that the Motion to make the complaint more definite and certain be and the same is hereby denied.

And, upon motion made in open court by the attorney for the defendant, to which no objection was raised by attorney for plaintiff;

It Is Ordered that there be a segregation of issues, and that the issue as to whether or not the claims of plaintiff set forth in his complaint are barred by the Statute of Limitations or by laches, be first determined, and that other issues be determined thereafter.

Dated at Portland, Oregon, this 29 day of November, 1943.

JAMES ALGER FEE

Judge

[Endorsed]: Filed Dec. 1, 1943. [12]

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[Title of District Court and Cause.]

ANSWER

First Defense

The complaint fails to state a claim against defendant upon which relief can be granted.

## Second Defense

Defendant admits the allegations of Paragraphs I and II of the complaint; denies all of the allegations of Paragraph III except he admits that in the fore part of December, 1930, he owned stock in the Western Bond & Mortgage Company and that there was a corporation organized under the laws of Oregon named the Western Guaranty Co. which was a subsidiary of Western Bond & Mortgage Company, and further admits that in December, 1930 he sold his stock in Western Bond & Mortgage Company, after which he was no longer a director, officer or stockholder of said corporation and that thereafter he purchased from Western Bond & Mortgage Company the stock of Western Guaranty Co.; denies all of the allegations of Paragraph IV, except he admits that somewhere about the time mentioned Western Bond & Mortgage Company owned some stock in Consolidated Credit Corporation, the details of which are no longer in the memory of defendant; denies all of the allegations of Paragraph V except the allegations about a tax claim by the U. S. Government against Western Bond & Mortgage Company and as to such allegations defendant says that he is [13] without knowledge or information sufficient to form a belief as to the truth of those allegations.

## Third Defense

The alleged right of action or rights of action set forth in the complaint did not accrue within



ten years next before the commencement of this action or within eight years after plaintiff and his predecessors in interest knew or in the exercise of reasonable diligence should have known of the facts connected with said transactions.

#### Fourth Defense

Plaintiff is barred from prosecuting this action by laches.

REILLY & DAVIDSON

Attorneys for Defendant

[Endorsed]: Filed Dec. 2, 1943. [14]

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[Title of District Court and Cause.]

#### PRE-TRIAL ORDER AND ORDER SEGREGATING ISSUES

This case came before this Court on Friday, April 14, and on Saturday, April 15, for pre-trial under the provisions of Rule 16 of Rules of Civil Procedure of the District Courts of the United States.

Plaintiff was represented by Sidney Teiser of Teiser & Keller, and defendant was represented by John F. Reilly of Reilly & Davidson. After preliminary discussion, which included the statement by counsel of their respective contentions, the parties, with the aid of the Court, undertook to determine what facts, if any, might be agreed upon, and what documents or writings might be admitted as

genuine, or copies of writings or documents might be accepted in lieu of the originals and admitted as genuine. Therefore, based upon said proceedings,

It Is Ordered that the following facts, having been agreed upon, may be considered at the trial as having been proven without the necessity of the introduction of any evidence concerning the same by either party.

### I. AGREED FACTS

1. On December 12, 1929, the defendant owned or controlled approximately two-thirds of all the voting stock of the Western Bond and Mortgage Company. On December 20, 1930, the defendant or the Laurel Investment Company owned in excess of five-sixths of the voting stock of the Western Bond and Mortgage Company. The defendant owned or controlled substantially [15] all of the stock of Laurel Investment Company on said latter date, and was its president. From December 12, 1929, to some time during the day of December 20, 1930, the defendant was a stockholder and president and director of the Western Bond and Mortgage Company.

2. That on the first day of December, 1930, the Western Bond and Mortgage Company caused the organization of a corporation known as the Western Guaranty Company, an Oregon corporation, with authorized capital stock of 500 shares, of the par value of \$10.00 each. At least two of the incor-

porators of the Western Guaranty Company were employees of Western Bond and Mortgage Company. The minutes of the Western Bond and Mortgage Company contain no reference to this incorporation of the Western Guaranty Company.

3. Under date of December 15, 1930, the books of the Western Bond and Mortgage Company record a transaction whereby assets carried on the books of the corporation were transferred to Western Guaranty Company for all of the stock of said company. The particular journal entries on the books of the Western Bond and Mortgage Company in reference to this transaction are as follows:

PLAINTIFF'S PRE-TRIAL EXHIBIT No. 6

WESTERN BOND & MORTGAGE CO.

Journal Entry Voucher

Date	Dec. 15, 1930		No. 49962
Account		Debit	Credit
Stock Purchase Liability.....	1,531,520.70		
Accrued Int. on Stock Sales.....	24,698.22		
Stock Sales—Oregon .....	213,156.59		566,265.00
“ “ —Washington .....	33,019.50		83,295.00
“ “ —Utah .....	9,275.15		28,065.00
“ “ —Colorado .....	35,103.17		99,285.00
“ “ —Montana .....	24,987.70		62,220.00
“ “ —Wyoming .....	20,175.38		49,080.00
“ “ —Idaho A.....	110,719.70		305,790.70
“ “ — “ C .....	73,441.40		177,010.00
“ “ —Misc. ....	58,496.96		160,510.00
Notes Payable—Consol. Cr. Corpn.....	161,478.00		
Profit Sales.....	84,585.85		

Account	Debit	Credit
Corpn. Stocks Owned—Western		
Guaranty Co.....	227,228.50	
Corpn. Stock Trusteed on		
Stock Sales.....		603,487.50
Def. Dis. on Stock Purchases		245,650.12
Corpn. Stock Owned—		
Consol. Cr. Corpn.....		40,008.50
Corpn. Stock Pl. on Notes Payable....		187,220.00
No record transfer of Conversion accounts to Western Guaranty Co. and to set up cost of stock of that company.		

Approved

I Hereby Certify That the  
Above Entry Is Correct

Auditor

M. D.

## DEFENDANT'S PRE-TRIAL EXHIBIT No. 5

## WESTERN BOND &amp; MORTGAGE CO.

## Journal Entry Voucher

Date Dec. 15, 1930

No. 49964

Account	Debit	Credit
Corpn. Stock Owned.....	10,200	
(West. Guar. Co.)		
Notes Payable (Consol. Cr. Co.....	7,000	
Corpn. Stock Owned.....		17200
(Baldy Finance Co.)		

To record additional cost of Western Guaranty Co. stock and to transfer Baldy Finance Co. stock.

Approved

I Hereby Certify That the  
Above Entry Is Correct

Auditor

M. D.

The minutes of the Western Bond and Mortgage Company contain no reference to this transaction.

4. That on or about the 20th day of December, 1930, defendant or Laurel Investment Company, or both, sold and transferred all their common or voting stock in the Western Bond and Mortgage

Company to Massachusetts Mortgage Company or to one E. F. O'Flynn, its president, receiving therefor the following:

(a) 100 shares of capital stock of Lake Lucerne Company, a Washington corporation, without par value.

(b) Conditional sales contract on automobiles, with unpaid balances amounting to \$22,661.03.

(c) Mortgage from Ljungdahl Products Co. to Massachusetts Mortgage Co., recorded in Records of Chattel Mortgage, Pierce County, Wash., amount of unpaid principal \$24,750.00.

(d) Note, W. I. Birwell to Massachusetts Mortgage Co. dated October 6, 1930, \$19,477.70.

(e) Note of Massachusetts Mortgage Co. to Laurel Investment Co. dated December 20, 1930, for \$87,000.00. [17]

5. That on December 20, 1930, at a special meeting of the directors, at which defendant presided, W. E. Johnson and E. F. O'Flynn were elected to fill two vacancies on the board of directors. The meeting then recessed for half an hour and re-convened, whereupon the resignation of defendant as director and president, and of V. Lyle McCroskey as director and secretary of the Western Bond and Mortgage Company having been tendered, were accepted. The Board of Directors then elected W. B. Johnson as president and E. F. O'Flynn as secretary-treasurer, and W. E. Johnson presided at the re-convened meeting and E. F.



O'Flynn acted as secretary. The following resolutions were thereupon adopted:

“Resolved that the President and Secretary be and they are hereby authorized and directed to transfer, assign and deliver to the Laurel Investment Company all of the capital stock of Western Guaranty Co. consisting of 500 shares of the par value of \$10.00 each and in exchange therefor to take an assignment and delivery of certain assets from the Laurel Investment Company, an itemized schedule of which is set forth in Exhibits “A” and “B” presented to this meeting and a copy of which is attached to the minutes hereof.”

(The assets listed in said exhibits consisted of the same assets as those referred to in (a) to (e), inclusive, of Paragraph 4 of Agreed Facts in this pre-trial order, except that the conditional sales contracts are itemized.)

“Further Resolved that it is the judgment of the directors that the assets received by this corporation in said exchange are of equal or greater value than those so to be assigned to Laurel Investment Company and that it is for the best interest of this corporation that said exchange be made.”

6. That on the 20th day of December, 1930, Laurel Investment Company transferred to the Western Bond and Mortgage Company the assets mentioned (set forth as a, b, c, d, and e in paragraph 4 of these Agreed Facts) and received from the Western Bond and Mortgage Company therefor all of

the capital stock of the Western Guaranty Company.

7. That on or about the 12th day of December, 1929, the Western Bond and Mortgage Company owned and held 40,000 shares of the Consolidated Credit Corporation Class A no par stock. [18]

8. That fee simple title to the property known as Russell Ranch (described more particularly in two deeds marked pre-trial exhibit 53 and 54) was in C. H. Russell on April 30, 1925, and that on said date C. H. Russell deeded the property to Russell Land & Livestock Company, which deed was recorded on May 4, 1925; that the Russell Land & Livestock Company held such property until December 20, 1929, when it deeded it to the Keystone Finance Company, and that the Keystone Finance Company held said property until February 13, 1932, when it deeded it to the Ochocho Farms Corporation, the latter deed being filed for record on May 2, 1932; and that an abstract of title to said property, if it were introduced at the trial, would show such title and such transfers, and none others during said period; and that at no time will an abstract of the title to said Russell Ranch show that E. C. Tapfer, F. A. Tapfer, or F. H. Snodgrass owned any interest in or to said Russell Ranch.

9. That on March 13, 1931, there was filed in the District Court of the United States for the District of Oregon, a complaint in equity, No. E-9189, wherein one John Brockie was plaintiff and

Western Bond and Mortgage Company, C. H. Farrington (the defendant herein), Laurel Investment Company, Western Guaranty Company, and others, were defendants. In said complaint many charges of misappropriations were made against this defendant and others. Among such many charges was one which made some reference to the transactions referred to in paragraphs 4, 5, and 6 of the Agreed Facts.

10. That the defendant herein filed an answer in said Brockie suit and the other defendants pleaded therein and the cause came on for trial before a referee appointed by said court. Plaintiff in said cause filed a motion for leave to dismiss said suit. That defendant resisted said motion. The motion was allowed but the plaintiff therein was ordered to pay all of the costs of all the parties, including the fees of the referee. Said suit was thereupon dismissed.

11. Thereafter and on July 14, 1931, one H. C. Thompson and other bond holders and stockholders of Western Bond and Mortgage Company filed a suit in the Circuit Court of the State of Oregon for Multnomah County, [19] against the Western Bond and Mortgage Company and others, but the said C. H. Farrington was not made a party in said suit.

12. Thereafter and in September, 1931, a suit was brought in the Circuit Court of the State of Oregon for Multnomah County wherein Edward Pape and sixteen other bondholders or creditors

of Western Bond and Mortgage Company were plaintiffs and the Western Bond and Mortgage Company and others were defendants, but in this case also C. H. Farrington was not made a party.

13. On or about November 25, 1931, a petition of certain creditors of Western Bond and Mortgage Company praying that said corporation be adjudged a bankrupt was filed in the United States District Court for the District of Oregon.

14. During the year 1934 and prior to the 20th day of July, 1934, the Corporation Department of the State of Oregon, at the instance and request of certain bondholders and stockholders of Western Bond and Mortgage Company investigated the affairs of Western Bond and Mortgage Company and intervened in said bankruptcy proceeding.

15. Plaintiff herein was appointed receiver of said corporation on August 13, 1934, and on December 12, 1934, was appointed Trustee in Bankruptcy of Western Bond and Mortgage Company; and he has acted in the capacity of said trustee ever since.

## II. DOCUMENTARY EVIDENCE

That the following exhibits submitted at the pre-trial by plaintiff or by the defendant may be received in evidence, without the necessity of proof as to their authenticity, but subject to all other objections, and where copies instead of originals are presented, such copies may be received in evidence as though they were originals.

## Plaintiff's Exhibits:

1. Eight stock certificates of Western Bond & Mortgage Company;
2. Letter dated January 12, 1931, Massachusetts Mortgage Company by N. Foley to W. E. Johnson;
3. Proxy issued to E. F. O'Flynn and signed Massachusetts Mortgage Co., by its Secretary;
4. Transfer from Laurel Investment Company to Western Bond and Mortgage Company, dated December 20th, 1930, with Exhibit "A" attached;
5. Journal Entry Voucher No. 49964 of Western Bond & Mortgage Co.
6. Journal Entry Voucher No. 49962 of Western Bond & Mortgage Co.
7. Certified copies of Articles of Incorporation and Annual Report for fiscal year ending June 30, 1931, of Western Guaranty Co.
8. Photostatic copy of Report of Examining Officer L. C. Gunning, dated October 19, 1932, with letter dated Nov. 8, 1932, signed by C. H. Farrington addressed to Internal Revenue Agent in Charge, Portland, Oregon, and photostatic copy of Protest of C. H. Farrington covering year 1930, attached;
9. Photostatic copy of Petitioner's Reply Brief in C. H. Farrington vs. Commissioner of Internal Revenue;



10. Minute book of Western Bond and Mortgage Company, with particular reference to minutes of meeting of December 20th, 1930, of stockholders, and of June 12th, 1930, of directors;

11. Photostatic copy of document dated September 19, 1932, C. H. Farrington to Commissioner of Internal Revenue, headed, "Protest";

12. Photostatic copy of Petition in case of C. H. Farrington, Petitioner, vs. Commissioner of Internal Revenue, before United States Board of Tax Appeals;

13. Photostatic copy of Answer in case of C. H. Farrington v. Commissioner of Internal Revenue;

14. Photostatic copy of Reply in same case;

15. Photostatic copy of decision in same case.

16. Journal Entry Voucher No. 53016, dated April 30, 1933;

17. Journal Entry Voucher No. 50618, dated May 21, 1931;

18. Journal Entry Voucher No. 50199, dated February 6, 1931;

19. Journal Entry Voucher No. 53015, dated April 30, 1933;

20. Certificate No. 9 of Ljungdahl Products Corporation for 250 shares of preferred stock to Western Bond and Mortgage Company, dated December 31, 1930, etc.

21. Certificate No. 3 for 2000 shares issued by Insurance Building Corporation to Massachusetts Mortgage Company, dated May 21, 1931;

22. Certificates No. 31 issued by Tacoma Products Co. for 15,706 shares of preferred stock to Western Bond & Mortgage Company, dated March 19, 1932; [21]

23. Letter dated April 5, 1933, Massachusetts Mortgage Co. to E. E. Gallagher;

24. Assignment of Mortgage from Western Bond and Mortgage Company to Tacoma Wood Products Company, dated April 1st, 1932;

24½. Carbon duplicate of last document, undated and unsigned;

25. Assignment of Mortgage from Western Bond and Mortgage Company to Lawyers Title and Trust Company, dated February 20, 1931;

26. Letter dated February 20, 1931, E. E. Gallagher, Western Bond and Mortgage Company, to Lawyers Title & Trust Co.

27. Receipt dated April 6, 1933, signed Western Bond and Mortgage Company, by E. E. Gallagher, showing receipt from Lawyers Title & Trust Company of mortgage of Tacoma Wood Products Company;

28. Note dated April 1, 1932, for \$24,750.00, executed by Tacoma Wood Products Company to Western Bond & Mortgage Company;

29. Mortgage from Tacoma Wood Products Company to Western Bond & Mortgage Company, dated April 1st, 1932;

30. Check dated May 4, 1933, signed by Assistant Manager of The Bank of California, payable to County Recorder, Pierce County, Wn., for \$1.50;

31. Letter dated March 21, 1933, Massachusetts Mortgage Company to Western Bond & Mortgage Co.

31A. Copy of letter attached to last above exhibit dated March 23, 1933, Western Bond and Mortgage Company to Massachusetts Mortgage Company;

32. Copy of letter dated June 17, 1933, Western Bond and Mortgage Company to M. Cleverly, c/o Massachusetts Mortgage Company;

33. Letter dated June 14, 1933, C. H. Renschler, County Auditor, to Western Bond and Mortgage Company, with envelopes attached;

34. Copy of letter dated June 15, 1933, Western Bond and Mortgage Company, to A. L. Kelly, Deputy County Auditor, Pierce County;

35. Letter dated June 7, 1933. M. Cleverly to Miss E. E. Gallagher;

36. Copy of letter dated May 3, 1933, Western Bond and Mortgage Company, to County Recorder, County of Pierce;

37. Letter dated May 5, 1933, C. H. Renschler, County Auditor, by A. L. Kelly, Deputy, to Western Bond and Mortgage Company;

38. Copy of letter dated May 9, 1933, Western Bond and Mortgage Company to Miss A. L. Kelly, Deputy, c/o County Auditor's Office, Pierce County; [22]

39. Letter dated May 10, 1933, C. H. Renschler, County Auditor, to Western Bond & Mortgage Company;

40. Letter (copy) dated May 17, 1933, on stationery of Western Bond & Mortgage Co., to M. Cleverly, Massachusetts Mortgage Company;

41. Duplicate copy of last above exhibit;

42. Letter dated May 16, 1943, M. Foley to "Dear Miss Gallagher";

43. Copy of letter dated June 2, 1933, Western Bond and Mortgage Company, to Miss M. Cleverly;

44. Note dated December 20, 1930, for \$87,000.00, payable to Laurel Investment Company, signed Massachusetts Mortgage Company, etc.;

45. Carbon copy of letter dated April 22, 1931, W. E. Johnson, President, to E. F. O'Flynn, etc.;

46. Journal Entry Voucher No. 43617 of Western Bond & Mortgage Co., dated December 12, 1929;

47. Western Bond and Mortgage Company Voucher No. G 75687;

48. Western Bond and Mortgage Company Voucher No. G 75686;

49. Minute Book of Keystone Finance Co.
50. Stock Book of Keystone Finance Company;
51. Document headed "Information Return of Subsidiary or Affiliated Corporation for calendar year 1928" of Russell Land & Livestock Company;
52. "Affiliations Schedule to be filed with each Consolidated Return," "Taxable year ended December 31, 1930," parent corporation Western Bond & Mortgage Company;
53. Deed between Russell Land & Livestock Co. and Keystone Finance Co., dated December 20th, A. D. 1929;
54. Deed from Russell Land & Livestock Co. to Keystone Finance Co., dated December 20th, A. D. 1929;
55. Book designated "Russell Land and Livestock Minute Book";
56. "Corporation Income Tax Return for Calendar Year 1929" by Western Bond & Mortgage Company and Affiliated Companies;
57. Capital stock ledger of Western Bond & Mortgage Co.
58. Certificate book of Western Bond and Mortgage Company;
59. Copy of letter dated May 27, 1943, from Treasury [23] Department, Washington, to Collector of Internal Revenue, Portland, etc.
60. Copy of letter dated May 7, 1943, from



Treasury Department, Washington, to Collector of Internal Revenue, Portland, etc.

103. Volume 1 of Transcript in case of The Bank of California, National Association, vs. George M. McBride, Trustee;

103-A. Volume 2 of Transcript, same case;

162. Credit file Bank of California -F.

Defendant's Exhibits:

61. By-Laws of Western Bond and Mortgage Company;

62. Copy of Complaint in case of John Brockie v. Western Bond & Mortgage Company, et al.;

63. Copy of article from Oregon Journal of March 13, 1931;

64. Copy of article from Portland Telegram of March 13, 1931;

65. Copy of article from The Oregonian of March 14, 1931;

66. Answer of Western Bond and Mortgage Company and Beacon Investment Company in case of John Brockie vs. Western Bond and Mortgage Company, et al.;

67. Answer of C. H. Farrington in last above case;

68. Motion to dismiss filed by plaintiff in above case;

69. Copy of memorandum of defendants Lau-

rel Investment Company, Western Guaranty Company and C. H. Farrington opposing motion of plaintiff to dismiss in above case;

70. Journal entry of this Court in said case on July 27, 1931;

71. Copy of order dismissing suit in last above case;

72. Copy of article from The Oregon Journal of July 13, 1931;

73. Copy of article from The Oregonian of July 14, 1931;

74. Copy of complaint in case of H. C. Thompson, et al, vs. Western Bond & Mortgage Company, et al, in Circuit Court of Oregon for Multnomah County; [24]

75. Copy of article from Oregon Journal of July 14, 1931;

76. Copy of article from The Oregonian of July 15, 1931;

77. Motion, with affidavit of Oscar Furuset attached, in case of Edward Pape, et al, v. Western Bond and Mortgage Co., et al, in Circuit Court of Oregon for Multnomah County;

78. Copy of article from Oregon Journal of July 19, 1934;

79. Copy of article from The Oregonian of Friday, July 20, 1934;

80. Article from Oregon Journal, Saturday, Au-

gust 4, 1934, and article from Oregon Journal of Monday, August 13, 1934;

81. Copy of article from Oregon Journal of August 14, 1934;

82. Copy of article from The Oregonian of August 4, 1934;

83. Copy of article from The Oregonian of August 14, 1934;

84. Copy of article from The Oregonian of August 19, 1931;

85. Copy of article from Oregon Journal of September 10, 1931;

86. Copy of amended complaint in H. C. Thompson, et al, vs. Western Bond & Mortgage Company, et al, in Circuit Court of Oregon for Multnomah County;

87. Copy of order of October 6, 1931, in last above case;

88. Copy of affidavit of Allen H. McCurtain in last above case;

89. Copy of amended petition in case of The Bank of California, N. A., vs. George McBride, Trustee of Western Bond and Mortgage Company;

90. Copy of Findings of Fact in last above case;

91. Copy of Motion of The Bank of California;

92. Copy of Affidavit of Harvey N. Black;

93. Copy of Affidavit of W. Lair Thompson;
94. Copy of Opinion of Judge Fee;
95. Copy of Order upon Motion to Rehear and Rehearing;
96. Copy of Testimony of E. E. Gallagher;
97. Copy of Testimony of R. Erickson;
98. Copy of Testimony of William Kennedy;
99. Copy of Testimony of Thomas G. Greene;
100. Copy of Colloquy between counsel;
101. Copy of Testimony of E. F. Munly;
102. Copy of Testimony of George M. McBride;
104. Copy of Order Authorizing Trustee to Retain Attorney in Matter of Western Bond & Mortgage Co., Bankrupt, No. B-16772, in District Court of United States for District of Oregon;
105. Copy of Petition for Order to Show Cause filed July 16, 1936, same Matter;
106. Copy of Order Appointing Counsel for Trustee in same Matter;
107. Copy of Petition for Approval of Agreement filed April 16, 1937, in same Matter;
108. Copy of Examination of Witnesses under Section 21-A, filed May 17, 1937, containing excerpts from testimony of Mr. William G. Brown and Dr. John H. Besson;
109. Copy of Order Confirming Agreement regarding Attorney's fees;

110. Copy of Order Directing Trustee to pay certain expenses;

111. Copy of Financial Report and Petition of Trustee;

112. Copy of letter dated July 20, 1936, R. Erickson to Sidney Teiser;

113. Copy of statement dated February 13, 1943, rendered by R. Erickson & Co. to George McBride, Trustee, amount \$2,500.00;

114. Copy of Order to pay Attorneys and Accountant, filed April 23, 1943;

115. 3 sheets, first bearing statement "(Standard Company)," and further statement "(Copy from 'Certified Valuation, Ljungdahl Products Co., Tacoma, Washington, Standard Appraisal Company'";

116. Copy of Appraisal of Lake Lucerne property;

117. Copy of Appraisal in re "Certified Valuation, Tahoma Apartments, Tacoma, Washington, Standard Appraisal Company";

118. Letter dated December 19, 1930, J. P. Gleason, Chairman, to C. H. Farrington, President, Western Bond & Mortgage Co.;

119. Journal Entry Voucher No. 43614;

120. Journal Entry Voucher No. 43615; [26]

121. Journal Entry Voucher No. 43616;

122. Journal Entry Voucher No. 43240;



123. Journal Entry Voucher No. 43665;
124. Journal Entry Voucher No. 49535;
125. Journal Entry Voucher No. 49640;
126. Journal Entry Voucher No. 49641;
127. Journal Entry Voucher No. 49643;
128. Journal Entry Voucher No. 49796;
129. Journal Entry Voucher No. 49963;
130. Journal Entry Voucher No. 49976;
131. Journal Page 6941;
132. Journal Page 7120;
133. Ledger sheet of Western Bond and Mortgage Company, "Sheet 1, Corporation Stocks Owned" and on other side "Sheet 2, Corporation Stocks Owned," with pencil memorandum attached;
134. Minutes of Special Meeting of Board of Directors of Western Bond and Mortgage Company held June 5th, 1930;
135. Waiver and relinquishment of payment of dividends dated July 1st, 1930, signed Tilla S. Farrington;
136. Waiver and relinquishment of payment of dividends signed Laurel Investment Company;
137. Waiver and relinquishment of payment of dividends dated July 1st, 1930, signed C. H. Farrington;

138. Waiver and relinquishment of payment of dividends dated July 1st, 1930, signed V. Lyle McCroskey;

139. Waiver and relinquishment of payment of dividends, signed by Oak Service Corporation, etc.

140. Waiver and relinquishment of payment of dividends dated July 1st, 1930, signed C. H. Farrington and Tilla S. Farrington;

141. Minutes of Special Meeting of Board of Directors of Western Bond and Mortgage Company held June 6th, 1930; [27]

142. Waiver of Notice of Directors Meeting of Western Bond and Mortgage Company, dated December 28th, 1930, signed C. H. Farrington, J. W. Latimer and V. Lyle McCroskey;

143. Minutes of Special Meeting of Board of Directors of Western Bond and Mortgage Company held December 20th, 1930;

144. Oath of Directors;

145. Resignation of V. Lyle McCroskey as Secretary-Treasurer and Director of Western Bond and Mortgage Company dated December 20, 1930;

14. Resignation as President and Director of Western Bond and Mortgage Company by C. H. Farrington, dated December 20, 1930;

147. Resignation as Assistant Secretary of Western Bond and Mortgage Company by E. Hagenbucher, dated December 20, 1930;

148. Photostatic copy of letter dated December

19, 1930, J. P. Gleason, Chairman, to C. H. Farrington, President, Western Bond and Mortgage Co., on stationery of American Exchange Bank of Seattle;

149. Continuation of Minutes of Special Meeting of Board of Directors of Western Bond and Mortgage Company, 2 pages;

150. Four pages typewritten matter, first page headed "Exhibit A," remaining three consisting of tabulations;

151. Oath of Director E. J. Boxer;

152. Journal Entries Aug. 1, 1929, to Jan. 1, 1930;

153. Journal Entries Jan. 1, 1930, to Jan. 1, 1931;

154. Journal Entries, Jan. 1, 1931, to Jan. 1, 1932;

155. Petition in Intervention in the matter of Western Bond & Mortgage Co., a corporation, In Bankruptcy, B. 16722.

156. Letter to I. H. Van Winkle, Attorney General, to Creditors, dated Nov. 24, 1934. [28]

157. Form of Proof of Claim and Power of Attorney;

158. Voucher, State of Oregon, in amount of \$490.85—2 pages.

159. Check in payment of voucher marked "Defendant's Pre-Trial Exhibit 158," (two pages);

160. Voucher, State of Oregon, in amount of \$900.00, (3 pages);

161. Check in payment of voucher marked "Defendant's Pre-Trial Exhibit 160."

162. Credit file of Bank of California.

[Marginal Note]: Amendment by order 12/6/44.  
By R De.

### III. CONTENTIONS OF PLAINTIFF

Plaintiff contends that:

C. H. Farrington, the defendant, defrauded the Western Bond and Mortgage Company, now bankrupt, of which company plaintiff, George M. McBride, is trustee in bankruptcy, in the manner and to the extent set forth in the following two claims:

#### First Claim

On or about the 20th day of December, 1930, C. H. Farrington acquired in exchange for his stock in the Western Bond and Mortgage Company of no value, certain assets of the Western Bond and Mortgage Company of the value of \$322,014.35, viz., the stock of the Western Guaranty Company, leaving the Western Bond and Mortgage Company holding, in lieu of said stock of the Western Guaranty Company, certain choses in action of practically no value.

Said Farrington acquired the said valuable Western Guaranty Company's stock in exchange for his worthless stock in the Western Bond and Mortgage Company by the following pre-arranged method and means:

Step 1. On December 1, 1930, while in control of the Western Bond & Mortgage Company, and while its president and director, and therefore while acting in a trustee capacity, C. H. Farrington caused, without authority so to do, to be organized a company known as the Western Guaranty Company, by office employees of the Western Bond and Mortgage Company and, without authority of the board of directors or stockholders, caused the Western Bond and Mortgage Company to subscribe to all of the stock of said Western Guaranty Company, par value \$5,000.00.

Step 2. On December 15, 1930, while acting in like capacity and while in like control, without any authority of the board of directors of the Western Bond and Mortgage Company, or of its stockholders, C. H. Farrington caused to be paid for the subscription of the Western Bond and Mortgage Company to the capital stock of the Western Guaranty Company certain assets of the Western Bond and Mortgage Company of a value of \$322,014.35; the Western Guaranty Company thereupon holding assets of the net value of \$322,014.35 and the Western Bond and Mortgage Company holding the stock of said Western Guaranty Company of like value.

Step 3. On December 20, 1930, C. H. Farrington, while acting in like capacity and while in like control, at a cost to him of \$5,000.00 commission, paid to a manipulator who had had frequent dealings in his [30] behalf, entered into an arrangement



whereby he, the said C. H. Farrington, transferred and conveyed all his stock and all of the stock which he controlled in the Western Bond and Mortgage Company (which was substantially all the outstanding voting stock in said company) to the Massachusetts Mortgage Company in exchange for certain securities or choses in action of doubtful if any value, viz.:

a. 100 shares non par stock Lake Lucerne Co. (a Washington corporation) par value \$100,000.00;

b. Conditional sale contracts on automobiles; face value \$22,661.03;

c. Mortgage from Ljungdahl Products Co. to Massachusetts Mortgage Co. recorded in records of Chattel Mortgage, Pierce County, Wash., Amount of unpaid principal \$24,750.00;

d. Note, W. I. Birwell to Massachusetts Mortgage Co. dated Oct. 6, 1930, face value \$19,477.70;

e. Note of Massachusetts Mortgage Co. to Laurel Investment Co. dated December 20, 1930, for \$87,000.00;

Step 4. On the same day, and practically simultaneously with his resignation as a director and president of the Western Bond and Mortgage Company, said C. H. Farrington transferred said valueless securities, through a corporation which he owned and controlled, (the Laurel Investment Company) to the Western Bond and Mortgage Company, and in exchange therefor obtained from the Western Bond and Mortgage Company the stock

of the Western Guaranty Company owned by the Western Bond and Mortgage Company of a value of \$322,014.35.

Thus, through the four steps above outlined, C. H. Farrington, while acting in the capacity of a trustee for said Western Bond and Mortgage Company, obtained property from it of a value of over \$300,000.00 in exchange for his stock in said company of no value, to the loss and damage of the Western Bond and Mortgage Company in the amount of \$322,014.35.

### Second Claim

On or about the 12th day of December, 1929, the Western Bond and Mortgage Company owned and held 40,000 shares of the Consolidated Credit [31] Corporation's Class A, no par stock, of a total value of \$120,000.00.

On or about said date, without any authority so to do, C. H. Farrington, then president and director of the Western Bond and Mortgage Company, and owner of approximately two-thirds of its common voting stock, and in control of said corporation, caused or permitted to be transferred out of said corporation and to a person or persons unknown, said 40,000 shares of said stock of the Consolidated Credit Corporation of the value of \$120,000.00.

Said Consolidated Credit Corporation's stock was transferred in purported consideration for all of the stock of a corporation known as the Keystone

Finance Company, but no such consideration was received for said stock since then and prior thereto the said stock of the Keystone Finance Company was already owned by the Western Bond and Mortgage Company.

Thus the Western Bond and Mortgage Company was defrauded by defendant, its president, director, and controlling stockholder, out of the value of said Consolidated Credit Corporation's stock, viz., the sum of \$120,000.00.

(Concerning Laches and the Statute of  
Limitations)

The plaintiff further contends that:

The enforcement of the above claims was timely sought in this court as soon as said facts on which they are based came to his knowledge, or by reasonable diligence could have come to his knowledge.

The facts on which such contention is made are:

Until a few weeks before the institution of this proceeding he had no knowledge or intimation of the particular transaction involving the Western Guaranty Company's stock (The First Claim), nor did he know or have any intimation of the particulars involving the disposal by the Western Bond and Mortgage Company of the 40,000 shares of Class A, no par value, stock of the Consolidated Credit Corporation (The Second Claim). [32]

The time, manner and circumstances under which he asserted knowledge concerning the facts above

set forth in his first and second claim herein were as follows:

The United States of America had filed a claim in bankruptcy for additional income taxes claimed to be due it by the Western Bond and Mortgage Company for the year 1930 in an amount which, with interest, exceeded \$50,000.00, and though such claim was filed by the United States of America in 1935, said claim was not pressed for hearing by the government until some time in the month of May, 1943, since no money in an amount sufficient to pay any appreciable portion of said claim came into the estate until slightly over a month before. Plaintiff, as Trustee, thereupon proceeded to investigate the claim asserted by the government for taxes so as to be able to file objections to same if such claim was subject to objections, and to contest the same at a hearing, if such claim were, in his opinion, improper. In order to obtain the data on which to make such objections and contest, the plaintiff, through his attorneys, made demand of the government of the United States, through its proper department, for a copy of the report of the agent on whose examination the additional tax assessment was made by the United States, since no copy of such report was found in the books, papers, and memoranda of the Western Bond and Mortgage Company turned over to him as trustee. On or about the 15th day of May, 1943, the United States Commissioner of Internal Revenue furnished to plaintiff's attorneys a copy of the revenue agent's revised report recommending additional assessment,

and on June 1, 1943, furnished to said attorneys copy of the revenue agent's original report. Upon reading said reports plaintiff became convinced that it would require the services of an accountant to delve into the facts of the situation touched upon in said reports, as well as into other matters which were pointed by such revenue agent's report, and accordingly he applied to the Referee in bankruptcy in charge of the bankruptcy estate for authority to employ a certified public accountant to make investigation [33] in regard to such matters and things. Authority was obtained from the Referee authorizing such employment. Plaintiff then employed as certified public accountant one Rudolph Erickson, and in due course of about two months, said certified public accountant informed him of matters on which objections to the claim of the government should be based, and likewise informed him of matters set up in the first and second claims set forth herein. Within a few weeks after said information was conveyed to him by said certified public accountant, and after causing examinations under Sec. 21-a of the Bankruptcy Act of various parties, he made further independent investigation and inquiries, and on or about the first day of October, 1943, having been convinced that fraud had been perpetrated herein, he made application to the referee in charge of the case for authority to institute suit against defendant herein, which authority was granted, and on the next day suit was instituted. Plaintiff had no knowledge or reason to believe of any delinquencies or improprie-



ties on the part of C. H. Farrington which would have led to a discovery of the facts set forth in plaintiff's first and second claims herein. He had a general knowledge that charges had been made and suits or actions brought both in the federal and state courts, against the Western Bond and Mortgage Company previous to his trusteeship herein in 1934, and that some charges in some of said suits or actions had been made against C. H. Farrington, but as to the nature and details of said charges plaintiff was not informed, nor did he have knowledge thereof, and plaintiff had a like general knowledge of the fact that several of the suits brought against the Western Bond and Mortgage Company and against said Farrington had been dismissed, though he did not know the specific charges which were made other than the fact that it was claimed that the Western Bond and Mortgage Company was insolvent and that a receivership of said company was being sought, nor did plaintiff have any further knowledge of such charges or of the facts set forth in his first and second claims herein until they were discovered by him in the manner herein above set forth. [34]

Thus, plaintiff brought suit within two years of the discovery of the fraud set forth in his first and second claims herein, and in fact brought suit speedily upon first discovery by him of such fraud, to-wit, in about thirty days thereafter.

## IV. CONTENTIONS OF DEFENDANT

Defendant denies all of the charges against him asserted by plaintiff, and contends that:

Defendant sold all of his stock in Western Bond and Mortgage Company on December 20, 1930, and thereafter had no participation whatever in the management of said corporation. That said corporation continued in active business under the control of its duly elected officers and directors until August 13, 1934, when plaintiff was appointed receiver thereof; that during said period defendant did not participate in any way in the operation or business of the said corporation.

During March, 1931, certain bondholders and stockholders of Western Bond and Mortgage Company caused one John Brockie, a stockholder of Western Bond and Mortgage Company, to file and the said Brockie did file in this court a suit wherein he made the same unfounded charges against this defendant as are made in this action by plaintiff and designated herein by plaintiff as claim No. 1 and other equally unfounded charges against this defendant were made in said Brockie suit general in their nature and not particularized.

Following the filing of said Brockie suit full publicity was given in the press of Portland and vicinity to said charges and at said time the plaintiff herein knew or should have known of said charges and that in any event the plaintiff had definite knowledge of the allegations in said suit not later than the year 1934.

Defendant answered said complaint in the Brockie suit giving full and accurate answer to all of the specific charges mentioned in said complaint, including the charges now made by the plaintiff and called by him his first claim, and other defendants in said suit likewise made full answer to said complaint. [35]

Defendant endeavored to get said case tried but against his vigorous opposition the plaintiff, Brockie, was permitted to discontinue said cause and dismiss said suit. That plaintiff knew or should have known at said time of the charges made in said suit and in any event had actual knowledge thereof not later than the year 1934.

At the time said case was pending in 1931 this defendant was in position to prove that all of his transactions with Western Bond and Mortgage Company were legitimate and that as to plaintiff's first claim that the assets transferred to Western Bond and Mortgage Company by Laurel Investment Company for the stock of Western Guaranty Company were of a value greatly in excess of the value of said Western Guaranty stock. That documentary evidence in support of said defense which was then in the files of Western Bond and Mortgage Company, but which the plaintiff asserts he is now unable to find, was then but is not now available and that witnesses who knew the facts were then living and now are dead.

On July 14, 1931, one H. C. Thompson and other bondholders and stockholders of Western Bond and

Mortgage Company filed a suit in the Circuit Court of the State of Oregon for Multnomah County against Western Bond and Mortgage Company and others, containing among other things the same charges against this defendant as are stated in plaintiff's first claim, and other general charges against this defendant, but this defendant was not made a party to said suit. Full publicity was given by the press of Portland and vicinity to the charges made against this defendant in said suit and the plaintiff herein knew or reasonably should have known thereof at the time and that he had definite knowledge thereof not later than the year 1934.

In September, 1931, a suit was brought in the Circuit Court of the State of Oregon for Multnomah County by Edward Pape and other bondholders and creditors of Western Bond and Mortgage Company against said Western Bond and Mortgage Company and others, which again reiterated the charges made against this defendant in the Brockie case, but again [36] this defendant was not made a party. Full publicity was given to the charges contained in said suit by the press of Portland and vicinity and the plaintiff herein knew or should have known thereof at the time, and in any event had definite knowledge thereof not later than the year 1934.

Various other actions and suits were brought against Western Bond and Mortgage Company during 1931, including an application made in November, 1931, by creditors of Western Bond and

Mortgage Company to have it adjudicated a bankrupt. These various lawsuits were publicized by the press and the plaintiff herein knew or should have known thereof at the time and in any event had definite knowledge thereof not later than the year 1934.

During the first half of 1934 the Corporation Department of the State of Oregon intervened in said bankruptcy and proceedings pending against Western Bond and Mortgage Company and an Assistant Attorney General and the District Attorney of Multnomah County investigated the affairs of Western Bond and Mortgage Company and conferred with attorneys representing the plaintiffs in the various suits heretofore referred to. At the instance of the Attorney General of Oregon this court appointed the present plaintiff receiver of Western Bond and Mortgage Company on August 13, 1934, and he immediately qualified by taking the necessary oath, and he was put in possession of all books, records and papers of Western Bond and Mortgage Company, and he has been in possession thereof ever since. That on December 12, 1934, Western Bond and Mortgage Company was adjudicated a bankrupt and the plaintiff herein was appointed trustee and since said date has been in possession of the books, records and papers of Western Bond and Mortgage Company as such trustee.

In March, 1935, plaintiff employed competent counsel to assist him and plaintiff and his said



counsel did or should have consulted auditors who had investigated the affairs of Western Bond and Mortgage Company for the various plaintiffs and for the Corporation Commissioner of Oregon, and plaintiff and his counsel did examine or should have [37] examined the books, papers and records of Western Bond and Mortgage Company, and did have or should have had as complete knowledge in the year 1935 of the affairs of Western Bond and Mortgage Company as they now have.

In June, 1936, plaintiff changed attorneys to his present counsel. In July, 1936, plaintiff secured the services of an accountant on a contingent fee basis. That said accountant did and does have offices with plaintiff's present counsel and is the same accountant as the one plaintiff now asserts he employed after June 1, 1943.

In April, 1937, plaintiff asked for and obtained approval of the Referee in Bankruptcy of a thirty-three and one-third per cent contingent fee agreement he had made with his present counsel to prosecute suits in various matters they had investigated with the aid of the accountant heretofore referred to.

Prior to July 1, 1936, plaintiff and his counsel had fully investigated the history of the Russell Ranch and of Keystone Finance Company and had prepared and filed documents alleging among other things that Western Bond and Mortgage Company was the owner of all stock of Keystone Finance Company, that said Keystone Finance Company

was a mere instrumentality of Western Bond and Mortgage Company, having no real corporate existence and seeking to recover the value of the Russell Ranch from the Bank of California, N. A.

Defendant contends that within a period of six months following his appointment as receiver and not later than one month after his appointment as trustee and in any event not later than July 1, 1935, plaintiff knew or in the exercise of reasonable diligence should have known all the facts relating to the actions of defendant as a director and president of Western Bond and Mortgage Company and his dealings with Western Bond and Mortgage Company in December, 1930, after he ceased to be a stockholder, director or officer of Western Bond and Mortgage Company. That plaintiff and his counsel had actual knowledge of the prior litigation and of the fact that numerous charges of misappropriation had been made against defendant [38] and were put on inquiry as to all of defendant's dealings and transactions with Western Bond and Mortgage Company and of all his actions while he was an officer and director of Western Bond and Mortgage Company.

Plaintiff is barred by the lapse of more than two years from the time plaintiff knew or should have known of the facts of the Western Guaranty transaction and of the fact that numerous other general charges had been made against defendant sufficient to put plaintiff on inquiry and that plaintiff is barred by the statute of limitations.

Plaintiff has been guilty of laches in failing to bring action while documentary evidence was available which is now no longer available, while witnesses who knew the facts were living who are now dead, and while the facts were within the memory of the witnesses still living.

## V. ISSUES OF FACT

The issues in dispute are:

(1) Did the acquisition from the Western Bond and Mortgage Company on or about December 20, 1930, of the stock of the Western Guaranty Company constitute a fraud on the part of the defendant for which recovery should lie, and if so, was Western Bond and Mortgage Company damaged thereby, and how much?

(2) Did plaintiff acquire actual knowledge of the facts on which plaintiff's first claim was based more than two years before this action was filed?

(3) Did the plaintiff, more than two years before this action was filed, acquire or should he have acquired knowledge or information which would have led him by the exercise of reasonable diligence to inquiry or investigation, and if said knowledge or information did or should have come to him and was or should have been pursued by him, would such pursuit have disclosed to him the facts on which plaintiff's first claim is based?

(4) Did defendant appropriate or is he chargeable with the appropriation or disposition of 40,-

000 shares of Class A no par value stock of the Consolidated Credit Corporation belonging to the Western Bond [39] and Mortgage Company, and if so, was the Western Bond and Mortgage Company damaged thereby, and how much?

(5) Did defendant acquire actual knowledge of the facts on which plaintiff's second claim was based more than two years before this action was filed?

(6) More than two years before this action was filed, did plaintiff acquire or should he have acquired knowledge or information which would have led him by the exercise of reasonable diligence to inquiry or investigation, and if such knowledge or information should have come to him and should have been pursued by him, should such pursuit have disclosed to him the facts on which plaintiff's second claim is based?

(7) If plaintiff is chargeable under Paragraph (3) or (6) with knowledge sufficient to bar the action on either his first or second claim, then would such knowledge so chargeable be sufficient to bar either or both of said claims?

## VI. ISSUES OF LAW

(1) Does the first claim of the complaint filed herein state a claim against the defendant?

(2) Does the second claim of the complaint filed herein state a claim against the defendant?

## VII. SEGREGATION OF ISSUES

In the interest of orderly proceeding and economy of time,

It Is Further Ordered that the issues raised herein be segregated and that the following issues be first tried and determined upon the facts, upon admissions, and upon the documents herein specified:

1. As to the first claim of plaintiff:

(a) Is the action barred by the Statute of Limitations or by plaintiff's laches?

(b) Did the plaintiff acquire actual knowledge of the transactions referred to in the plaintiff's first claim of the complaint more than two years before this action was filed? [40]

(c) Did plaintiff, more than two years before this action was filed, acquire or should he have acquired knowledge or information which would have led him by the exercise of reasonable diligence to inquiry or investigation and, if such knowledge or information would or should have come to him, and was or should have been pursued by him, should such pursuit have disclosed to him the facts on which plaintiff's first claim is based?

2. As to the second claim of plaintiff:

(a) Is this action barred by the Statute of Limitations or by plaintiff's laches?

(b) Did the plaintiff acquire actual knowledge



of the transactions referred to in the plaintiff's second claim of the complaint more than two years before the action was filed?

(c) Did the plaintiff, more than two years before this action was filed, acquire or should he have acquired knowledge or information which would have led him by the exercise of reasonable diligence to inquiry or investigation and, if such knowledge or information would or should have come to him and was or should have been pursued by him, should such pursuit have disclosed to him the facts on which plaintiff's second claim is based?

3. As to either or both claims of plaintiff:

If plaintiff is chargeable under Paragraph 1(c) or 2(c) above with knowledge sufficient to bar the action on either his first or second claim, then would such knowledge so chargeable be sufficient to bar action on the other claim?

It Is Further Ordered that, as to the other issues of fact and of law set forth herein, the same be subject to further pre-trial conference and that the determination of said other issues be postponed until further direction of this court.

Dated at Portland, Oregon, this 28th day of November, 1944.

JAMES ALGER FEE,  
Judge.

[Endorsed]: Filed November 28, 1944. [41]

[Title of District Court and Cause.]

### OPINION

This is an action by the trustee in bankruptcy of the Western Bond and Mortgage Company, a petition for the bankruptcy of which was filed November 24, 1931, in involuntary proceedings. The Western Bond and Mortgage Company was adjudicated on this petition September 24, 1934.

Certain transactions which occurred between the bankrupt and defendant Farrington who was an officer thereof are said to have transferred assets of that corporation to him without any consideration. These transactions are said by plaintiff to have occurred on the 20th day of December, 1930, as to the first "cause of action", and on the 12th day of December, 1929, as to the second "cause of action." They are alleged in the complaint to have been discovered on the 21st day of September, 1943.

McBride was appointed trustee of the Western Bond & Mortgage Company, bankrupt, on December 12, 1934. This action was commenced October 2, 1943. McBride is an attorney and has been chief of the estate tax department and of the income tax department of the United States Bureau of Internal Revenue. While so connected, he had some familiarity with the income tax liability of bankrupt and Farrington. He personally [42] heard some of the testimony at the trial of Farrington's case before the Board of Tax Appeals and was present at the taking of depositions of Brown and Besson in the bankruptcy court in 1931, which

transactions related to manipulations of the stock and property of the bankrupt.

Soon after his appointment as trustee, McBride was visited by Ralph Moody who was conducting an investigation of the affairs of bankrupt on behalf of the State Attorney General's office. From this source, McBride was paid a monthly sum for carrying on an investigation and furnished the services of two auditors. Latourette, attorney for McBride during this period, testified that strenuous efforts were made to investigate everyone who had been involved in the transactions resulting in bankruptcy, including Farrington. The newspapers carried accounts of the alleged civil and criminal liability of Farrington, some of which McBride had called to his attention, and there were many suits filed in court which contained positive allegations in relation thereto.

In 1935, McBride knew of a tax claim asserted by the Internal Revenue Department. He had known of the fact that there was an amended income tax return upon which, when he finally obtained a copy in 1943, he found bodied forth completely the foundation of this case. After he knew an income tax report existed, McBride called at the office of the agent of Internal Revenue but found no copy there. Sometime after this, he heard that Robert Jacob, an attorney, had a copy of this document. For three or four years after he had this knowledge, he made no effort to see the report. Finally, he called at Jacob's office. He found that

Jacob was out of the office and immediately abandoned all further effort. Thus he procrastinated for all these years in obtaining the copy although from his [43] experience in tax matters, he must have known that this document would have been invaluable in unwinding the tangled skein which he had in his hands. The whole theory of excusing the trustee for failure to bring this suit earlier is that the finding of this report and the amended return was the discovery of fraud.

In 1936, McBride employed Erickson, the present accountant, and about that time, present counsel were employed. Data was at hand pointing clearly to a loss of assets in another transaction. This was pursued with energy and ability by counsel for McBride both in this court, *In re Western Bond & Mortgage Company*, 44 F. Supp. 89, and in the Circuit Court of Appeals, *Bank of California National Association vs. McBride*, 132 F. 2d 469, with the result that there was a substantial recovery. The final opinion upon appeal was announced January 14, 1943. Thereafter, the energy theretofore concentrated on that case was transferred to this investigation with the result that the obvious means of obtaining the amended return were exercised and the alleged fraud was discovered.

The State Statute of Limitations in Oregon, on a fraud action, as this is, commences running from the date of the act and creates a bar within two

years, but provides that this period shall run only from discovery, either at law or in equity.<sup>1</sup>

In this case, the trustee is not suing to recover the property of the bankrupt in specie.<sup>2</sup> Nor is

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<sup>1</sup>Chapter 2, Title I, of the Oregon Statutes provides: “#1-201. Time of commencing actions: Objection, how taken. Actions at law shall only be commenced within the periods prescribed in this title, after the cause of action shall have accrued; \* \* \*

“#1-202. \* \* \* The periods prescribed in the preceding section for the commencement of actions, shall be as follows: \* \* \*

“#1-206. Within two years. Within two years—(1) \* \* \* for any injury to the person or rights of another, not arising on contract, and not herein especially enumerated; provided, that in an action at law based upon fraud or deceit, the limitation shall be deemed to commence only from the discovery of the fraud or deceit.”

“#9-103. A suit shall only be commenced within the time limited to commence an action as provided in Chap. 2, of Title I of this Code \* \* \*. In a suit upon a new promise, fraud or mistake, the limitation shall only be deemed to commence from the making of the new promise or the discovery of the fraud or mistake \* \* \*.” [44]

<sup>2</sup>Sections 70a and 70c are not antagonistic as contended by plaintiff. By Subsection (a) the trustee acquired all the rights which the bankrupt had in property which he had transferred in defraud of creditors. By the former section 47a(2) the trustee was given the rights of creditors as to all the property with which he became vested by virtue of the clauses of section 70. Under the act of 1938, all these provisions now become a part of section 70 and the causes of confusion no longer exist. (See 11 USCA #110, supp.)



it believed that this action is for injury or detention of the property of the bankrupt<sup>3</sup>. If a cause of action were given to the trustee by the Bankruptcy Act, the right would be generated by the terms of the enactment and would then fall within the two year limitation. The reasoning of *Herget vs. Central National Bank and Trust Company*, No. 322, October Term, 1944, January 29, 1945, . . . . . U. S. . . . ., would furnish an analogy. But if the cause of action is not given by the Act, as the better argument suggests, it must have been an inherited right. The cause of action is for fraudulently depriving the corporate bankrupt of certain property. Such a right can have a genesis in three ways in order for the trustee to inherit. First, a creditor of bankrupt might have rights against the person fraudulently obtaining such property.<sup>4</sup> Second, the bankrupt corporation itself might have a right against a person who fraudulently misappropriated its property. Finally, a stockholder might have a right of action for misappropriation, or breach of trust, by one of the officers of the corporation.<sup>5</sup> The court is of opinion that the present action is one derived from one of the above mentioned

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<sup>3</sup>"rights of action arising upon contracts, or usury, or the unlawful taking or detention of or injury to his property." Bankruptcy Act, §70a(6). A two year statute of limitations under the Oregon State Law would apply were the cause of action one for taking or detention of property.

<sup>4</sup>*Kane vs. Sesac*, 54 F. Supp. 853.

<sup>5</sup>See *In re Globe Drug Co.*, 9 Cir. 104 F. 2d 114.



sources. It does not take its initial genesis by virtue of the provisions of the Bankruptcy Act.<sup>6</sup>

Before the passage of the Act of 1938, it had been consistently held in the Ninth Circuit that to such an inherited cause of action the general statute of limitations prescribed by the particular state applied.<sup>7</sup> This was the more logical since it is a principle agreed upon with unanimity that where a right of action given by a particular state was conditioned in the same statute by a limitation, the expiration of the period thus set would bar the remedy, notwithstanding the language of the old clause 11d.<sup>8</sup> Universally the courts maintained that where the general law of the state had provided the right in a creditor, that if the law of the general limitation set up by the state had barred the remedy in the creditors, the trustee could not revive it.<sup>9</sup> This was founded upon the proposition that the trustee was enforcing a right based upon rights inherited from the bankrupt, or the creditors, and for which remedies were given by state law.<sup>10</sup> It

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<sup>6</sup>Cf. Section 60, Bankruptcy Act; 11 USCA §96; *Herget vs. Central National Bank & Trust Company*, *supra*. [45]

<sup>7</sup>*Davis vs. Willey*, 263 F. 588; *Davis vs. Willey*, 9 Cir. 275 F. 397.

<sup>8</sup>Bankruptcy Act of 1898, a 11d.

<sup>9</sup>See *Heffron vs. Duggins*, 9 Cir. 115 F. 2d 519; *Durrett vs. Harris*, 148 Arkansas 4, 228 S.W. 386; *Harrigan vs. Bergdol*, 270 U. S. 560.

<sup>10</sup>See *Davis vs. Willey*, *supra*; *Woodman vs. Butterfield*, 116 Maine 241; *Cobb vs. First National Bank*, 263 F. 1000; *First Presbyterian Church of Santa Barbara, Cal. vs. Rabbitt*, 118 F. 2d 732.

has been intimated that the former provisions of the Bankruptcy Act had no effect upon this situation since former section 11d was a withdrawal of juridicial and representative capacity.<sup>11</sup> Therefore, that section was not intended as a statute of limitations, but simply a termination of power. There were, it is true, cases holding that old section 11d was a true statute of limitations and if the remedy of a creditor were alive on the date of filing the petition, it lingered on available to the trustee until two years after final closing.<sup>12</sup> But practical considerations as well as authority constrain this court to the opposite view. Repose is the aim of those local statutes and the state policy should control. While then a case can be made for the retention of the remedy until a trustee could orient himself before bringing action, it should not be extended as in this case to thirteen years unless the affirmative policy of the state permit.

The state statute as above noted erected the bar of limitations against the remedies here sought sometime in 1933, unless the fraud was not discovered until later. But the trustee here had knowledge of facts sufficient to lead him to make the

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<sup>11</sup>See *Nairn vs. McCarthy*, 9 Cir. 120 F. 2d 910, where it is said: "It does not follow from the fact that the trustee is prohibited from bringing an action subsequent to that time that he is authorized to maintain an action prior thereto, irrespective of an applicable limitation statute." [46]

<sup>12</sup>*Isaacs vs. Neece*, 5 Cir. 75 F. 2d 566; *Engelbreton vs. West*, 133 Nebraska 846; 277 N.W. 433; *Callaghan vs. Bailey*, 293 N.Y. 396.

allegations presented here, soon after he assumed responsibility<sup>13</sup> for the management of the estate. Farrington bulked large in the rumors of fraudulent dealings with bankrupt in the whole period after the filing of the petition and covering the time of the initial incumbency of the trustee. The associates of the trustee indicate knowledge of it. The press accounts, at least one of which was specifically brought to the attention of the trustee himself, are full of such suspicions. There was litigation of record which pointed to these very transactions. All the records of the bankrupt were placed in the trustee's hands and he had some assistance and sufficient money to make an investigation of them. The mere fact that the trustee did not have the specific document, an amended income tax report for the year 1930, now considered to furnish conclusive proof, is immaterial. There was data on hand from which he should have taken warning of the essentials. The information was within the knowledge of the trustee before 1936, by construction. Such knowledge must be attributed to the trustee and his attorneys in that year which saw the first vigorous attempts to follow up the claim against the Bank of California. But two years had expired after these events before the Chandler Act took effect. Their action was barred then, by the Oregon statute, before the new act became effective.

Logically the opinion should stop here, but the

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<sup>13</sup>*Linebaugh vs. Portland Mortgage Co.*, 116 Ore. 1, 13, 14; Cf. *Sedlak vs. Sedlak*, 14 Ore. 540. [47]

arguments have wandered far afield. In order to save question, the court now considers the situations which would have arisen if knowledge had been obtained by the trustee at a later date.

If it be assumed that knowledge had not been obtained by the trustee by the date of the taking effect of the amendment to the bankruptcy law, in 1938, the two years after adjudication had already passed so that the particular clause of the statute gives no aid. But the state statute might give two years more vicariously. The court holds that the knowledge of facts which the trustee had during these two years was sufficient to guide him to an actual knowledge of the matters now alleged. Therefore, two years from the effective date of the Chandler Act barred the right of action completely. The question as to construction, if this action had been filed within two years from the effective date of the amendatory act, might have been puzzling, but that cannot arise now.

The Act of 1938 changed the whole situation with regard to limitations under the bankruptcy act. The conflict between the courts regarding the interpretation of the old section 11d was "primarily responsible for the framing of the new Section 11e in 1938."<sup>14</sup> The new section 11e was obviously a compromise and extended the limitations laid down by the state statutes under the interpretation of *Davis vs. Willey*, *supra*, to a fixed period of two

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<sup>14</sup>*Herget vs. Central National Bank & Trust Co.*, *supra*. [48]

years beyond the date of adjudication. It will be noted, however, that if the state statute had barred the action before the filing of the petition in bankruptcy, or if the state statute provided for a term of limitation which did not lapse until two years after adjudication, then no change was effected where the doctrines previously announced by the Ninth Circuit Court of Appeals continue in effect.<sup>15</sup> The purpose of the new act seems unquestionably to be to extend to the trustee a fixed period within which he might file all suits which he has inherited from the debtor unless it were the policy of the particular state to give him even a longer time.<sup>16</sup> Section 6 of the Bankruptcy Act of 1938, 11 U. S. C. A. §1, note, provides in part:

“Except as otherwise provided in this amendatory Act, the provisions of this amendatory Act shall govern proceedings as far as practicable in cases pending when it takes effect; but proceedings

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<sup>15</sup>In *Hastings vs. H. M. Byllesby & Co.*, 293 N.Y. 413, 57 N.E. 2d 537, the court cites and follows *Callaghan vs. Bailey*, *supra*, and thus comes to the conclusion that a diminution rather than an extension of the period of limitation was effected by new Section 11e of the bankruptcy act. From this premise the court arrives at the conclusion that it is not practicable to apply the new section of the Chandler Act. Although the reasoning of this distinguished court is persuasive, it is not binding here. The opinion simply means that in the state courts of New York a longer period of limitation will be applied. A court bound by *Davis vs. Willey*, *supra*, must necessarily reach a contrary conclusion.

<sup>16</sup>Cf. *Herget vs. Central National Bank & Trust Co.*, *supra*. [49]



in cases then pending to which the provisions of this amendatory Act are not applicable shall be disposed of conformably to the provisions of said Act approved July 1, 1898, and the Acts amendatory thereof and supplementary thereto.”

Inasmuch as the limitation clause is an extension rather than a diminution of the time allowed to the trustee for filing a cause which he has inherited from the bankrupt, it is practicable to apply new section 11e in this case. According to the determinations which the court has heretofore made upon the facts, the state statute already had run before the Chandler Act was enacted. Thus we are brought back to the same situation. It was practicable to apply the Chandler Act and to give effect to the state statute of limitations by the court as already found. Based on the facts, the remedy is barred.

Entirely irrespective of the limitations, state or federal, in a court of bankruptcy which is controlled by equitable principles, it would seem that the doctrine of laches was applicable.<sup>17</sup> It has, in fact, been applied in state courts under similar circumstances.<sup>18</sup> Even if we assume all of the allegations of plaintiff's complaint to be true, it still must be remembered that these actions were consum-

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<sup>17</sup>See *Wilkinson vs. Livingston*, 8 Cir. 45 F. 2d. 465.

<sup>18</sup>*Wolpert vs. Gripton*, 213 Cal. 474, 2 F. 2d 767; Cf. *Bovay vs. H. M. Byllesby & Co.* (Del. Ch. 1940) 22 A. 2d 138; also *Fredericks vs. Jacoby*, 128 N.Y. Eq. 426, 16 A. 2d 809.



mated in 1929 and 1930, approximately fifteen years ago; that the filing of the petition in bankruptcy was in 1931; that extensive investigations were made at that time; and that the main actors in the transactions with the exception of defendant, are dead, as well as others who have known material facts.<sup>19</sup> This court has allowed recovery upon another one of the major claims and this determination was affirmed by the Circuit Court of Appeals and the property has now been recovered. The right of recovery in that case was not nearly so clear at the outset as it appears now when opinions are on record, but after all, it represented even at that time, by far the best chance of upsetting a fraudulent transaction and obtaining money for this estate. The trustee and the present attorneys have devoted years of unflagging zeal to obtaining recoveries in that case, but it is the opinion of the court that they deliberately spent their work and efforts upon that proposition as the main chance and that they did not as vigorously pursue the clues that might have lead to a like recovery in the instant cause. There were sufficient facts of record long ago to have accomplished this purpose. All they had to do was to obtain the income tax return which they now have, and it was available to them at all times. Laches is not established by the lapse of time alone, but here there is detriment to the defendant in that he has been robbed of a means of defense by the death of witnesses and partici-

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<sup>19</sup>*Wilkinson vs. Livingston, supra*; Cf. *Bingaman vs. Commonwealth Trust Co.*, 15 F. 2d 119. [50]

pants, and on the other hand it is apparent to the court that there was a more or less deliberate choice in pursuing the other claim rather than this one. Whether these circumstances be used to create a bar by reason of laches, or to make plain that it is "practicable" to apply the provisions of the limitations in the Act of 1938, the result is impregnably established thereby. A bar to prosecution of these claims is now complete.

Findings and judgment of dismissal may be prepared.

Endorsed: Filed April 18, 1945. [51]

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[Title of District Court and Cause.]

## FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above cause came on for hearing before the Hon. James Alger Fee, Judge of the above Court, without a jury, on November 28, 1944, plaintiff appearing in person and by Sidney Teiser, one of his attorneys, and defendant appearing in person and by John F. Reilly and Stephen E. Parker, his attorneys, and the parties having theretofore agreed upon a pre-trial order and an order segregating the issues between the parties and said pre-trial order and order segregating the issues having been signed by the court, this cause was tried on the issues of the statute of limitations and laches and the parties having submitted evidence in sup-

port of their respective contentions and argued and submitted the matter to the Court, the Court now makes the following

## FINDINGS OF FACT

### I.

The transactions referred to in the complaint herein and the pre-trial order are alleged to have occurred in December, 1929 and December, 1930.

### II.

Plaintiff was appointed trustee in bankruptcy of Western [52] Bond and Mortgage Co. on December 12, 1934, and all of the records of said corporation were promptly placed in his hands, including a litigation record pointing to the transactions on which plaintiff bases his claims against defendant.

### III.

Prior to 1936 plaintiff had actual knowledge or was in possession of information which was sufficient to guide him to actual knowledge of the matters alleged in the complaint.

### IV.

Plaintiff failed to pursue with reasonable diligence the information which had come into his possession prior to 1936 and which pointed to the transactions referred to in the complaint.

### V.

This action was commenced on October 2, 1943.

## VI.

Prior to the bringing of this action participants in the transactions referred to in the complaint and others who had known the material facts had died and defendant was deprived of a means of defense through their evidence.

Based on the foregoing Findings of Fact the Court now makes the following

## CONCLUSIONS OF LAW

## I.

This action is barred by the provisions of Oregon Compiled Laws Annotated Sections 1-201 to 1-206 and Section 9-103.

## II.

This action is barred by the laches of the plaintiff.

## III.

Defendant is entitled to a judgment of dismissal with costs. Dated this 28th day of April, 1945.

JAMES ALGER FEE

District Judge

[Endorsed]: Filed April 28, 1945. [53]

In the District Court of the United States for the  
District of Oregon

Civil No. 2202

GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Co., an Ore-  
gon corporation, Bankrupt,

Plaintiff

v.

C. H. FARRINGTON,

Defendant.

### JUDGMENT OF DISMISSAL

The above cause came on for hearing before the Hon. James Alger Fee, Judge of the above Court, without a jury, on November 28, 1944, plaintiff appearing in person and by Sidney Teiser, one of his attorneys, and defendant appearing in person and by John F. Reilly and Stephen E. Parker, his attorneys, and the parties having theretofore agreed upon a pre-trial order and an order segregating the issues between the parties and said pre-trial order and order segregating the issues having been signed by the court, this cause was tried on the issues of the statute of limitations and laches and the parties having submitted evidence in support of their respective contentions and argued and submitted the matter to the Court, and the Court having heretofore filed its Findings of Fact and Conclusions of Law herein,

Now Therefore, based on said Findings of Fact and Conclusions of Law,

It Is Ordered and Adjudged that this action be and the same is hereby dismissed with prejudice and that defendant have and recover from plaintiff his costs and disbursements herein.

Dated this 28th day of April, 1945.

JAMES ALGER FEE

Judge.

[Endorsed]: Filed April 28, 1945. [54]

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[Title of District Court and Cause.]

### NOTICE OF APPEAL

Notice Is Hereby Given that George M. McBride, Trustee in Bankruptcy of Western Bond and Mortgage Company, an Oregon Corporation, Bankrupt, plaintiff above named, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit, from a Judgment of Dismissal entered in this action on the 28th day of April, 1945.

TEISER & KELLER

SIDNEY TEISER

Attorneys for Appellant

[Endorsed]: Filed May 28, 1945. [55]



[Title of District Court and Cause.]

DESIGNATION OF CONTENTS OF RECORD  
ON APPEAL

Plaintiff and Appellant hereby designates the following papers, documents and transcripts as the records proceedings and evidence to be contained in the record on appeal, being the entire record herein:

1. Complaint
2. Motion (to Dismiss and to make more Definite and Certain)
3. Order upon above motion
4. Answer
5. Pre-trial Order and Order Segregating Issues
6. Transcript of Testimony and Proceedings, including exhibits introduced, Nov. 28-29. Dec. 6, 1944.
7. Opinion
8. Findings of Fact and Conclusions of Law
9. Judgment of Dismissal
10. Notice of Appeal
11. This Designation of Contents of Record on Appeal
12. Order to send original exhibits.

TEISER & KELLER

SIDNEY TEISER

Attorney for Plaintiff and  
Appellant

United States of America

State of Oregon

County of Multnomah

Due service of the within designation hereby accepted in Multnomah County, Oregon, by receiving a copy thereof duly certified.

JOHN F. REILLY

Attorney for Defendant

May 31, 1945.

[Endorsed]: Filed May 31, 1945. [56]

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[Title of District Court and Cause.]

DEFENDANT'S DESIGNATION OF ADDITIONAL PORTIONS OF RECORD TO BE INCLUDED IN RECORD ON APPEAL

Defendant and respondent hereby designates the following additional portions of the record, proceedings and evidence to be included in the record on appeal:

- (1) All exhibits received or offered on the trial.
- (2) All of the proceedings on the hearing held March 30, 1945.
- (3) Bond on appeal, if any.

(4) Statement by appellant of the points on which he intends to rely.

/s/ CARL E. DAVIDSON

/s/ JOHN F. REILLY

Attorneys for Defendant and  
Respondent.

[Endorsed]: Filed June 6, 1945. [57]

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[Title of District Court and Cause.]

### ORDER

This cause having come on this day to be heard upon the motion of plaintiff for an order directing that the original exhibits be sent to the appellate court in lieu of copies, and it appearing to the court that a Notice of Appeal has been filed herein, and the court being of the opinion that the appellate court should have the original exhibits for inspection on such appeal:

It Is Ordered that all the original exhibits offered or received in evidence in this court be sent by the clerk of this court to the Circuit Court of Appeals for the Ninth Circuit in lieu of copies thereof, and

It Is Further Ordered that the sending of said originals in lieu of copies shall in no way be construed to indicate which of said exhibits shall or

shall not be printed in the printed Transcript of Record on Appeal.

Dated this 27th day of July, 1945.

JAMES ALGER FEE

Judge

O. K. JOHN F. REILLY.

[Endorsed]: Filed July 27, 1945. [58]

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CERTIFICATE OF CLERK

United States of America,

District of Oregon—ss:

I, Lowell Mundorff, Clerk of the District Court of the United States for the District of Oregon, do hereby certify that the foregoing pages numbered 1 to        inclusive, constitute the transcript of record on appeal from a judgment of said court in a cause therein numbered Civil 2202, in which George M. McBride, Trustee in Bankruptcy of Western Bond and Mortgage Company, an Oregon Corporation, Bankrupt, is plaintiff and appellant, and C. H. Farrington is defendant and appellee; that the said transcript has been prepared by me in accordance with the designations of contents of the record on appeal filed by the appellant and the appellee, and in accordance with the rules of this court; that I have compared the foregoing transcript with the original record thereof and that it is a full, true and correct transcript of the record and pro-

ceedings had in said court in said cause, in accordance with the said designations as the same appear of record and on file at my office and in my custody.

I am also enclosing herewith duplicate transcript of testimony and proceedings of November 28, 29 and December 4, 1944, and duplicate transcript of proceedings of March 30, 1945, together with exhibits 59, 60, 62 to 67, 69 to 73, 75, 76, 78 to 104, 106 to 112, 155 to 158, 160 and 162. Also pre-trial exhibit 77.

I further certify that the cost of comparing and certifying the within transcript is \$38.05 and that the same has been paid by the appellant.

In Testimony Whereof I have hereunto set my hand and affixed the seal of said court in Portland, in said District, this 30th day of July, 1945.

[Seal]

LOWELL MUNDORFF,  
Clerk.

By F. L. BUCK

Chief Deputy. [59]

[Title of District Court and Cause.]

TRANSCRIPT OF TESTIMONY

Portland, Oregon,  
November 28, 1944,  
10:00 o'clock A. M.

Before:

Honorable JAMES ALGER, FEE, Judge

Appearances:

Messrs. TEISER & KELLER (by Mr. Sidney Teiser), Attorneys for Plaintiff.

Messrs. REILLY & DAVIDSON (by Mr. John F. Reilly and Stephen E. Parker), Attorneys for Plaintiff.

Court Reporter:

IRA G. HOLCOMB.

PROCEEDINGS

The Court: Although I am somewhat familiar with the pre-trial order, I assume we should now, just on the eve of [1\*] trial, make up our minds as to whether there is anything further that should be done. Are both parties satisfied now with the pre-trial order?

Mr. Reilly: The defendant is satisfied.

Mr. Teiser: We are satisfied, sir.

The Court: You may then proceed. The Court will sign the pre-trial order at this time and place it of record.

Mr. Teiser: If your Honor please, I take it that it is not necessary to make any preliminary state-

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\*Page numbering appearing at top of page of original Reporter's Transcript.



ment at this time, as we have made our preliminary statements heretofore.

The Court: Yes.

Mr. Teiser: Under the provisions of the pre-trial order, we are now, according to my understanding, to engage only in the question as to whether or not the Trustee is bringing the suit within the time permitted by law or has, by laches, been precluded from bringing the suit.

The Court: As I understand, that is the first issue.

Mr. Teiser: Mr. McBride, will you take the stand, please?

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GEORGE M. McBRIDE,

the plaintiff herein, was thereupon produced as a witness in his own behalf and, being first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Teiser:

Q. Your name is George M. McBride? [2]

A. Yes.

Mr. Teiser: If your Honor please, for the purpose of clarity, I might call attention to the fact that it is one of the agreed facts that Mr. McBride is the regularly qualified and acting Trustee in Bankruptcy of the Western Bond and Mortgage Company, and is now acting in that capacity.

The Court: Yes.

(Testimony of George M. McBride.)

Q. You are the George M. McBride who is the Trustee in this case?      A. Yes sir.

Q. What is your occupation, or, what was your occupation at the time of your appointment as Receiver and Trustee?      A. I was an attorney.

Q. An attorney?      A. An attorney at law.

Q. Are you still engaged in the practice of law?

A. No.

Q. What is your occupation now?

A. I work for one of the shipbuilding companies.

Q. When did you first obtain any knowledge of controversies existing between the Western Bond and Mortgage Company and its bondholders, or creditors, or anyone else?

A. Well, at the time of my appointment as Trustee. That was in 1934.

Q. Trustee or receiver? [3]

A. No, it was receiver. I was appointed receiver on August 13, 1934.

Q. When was information brought to you, and how, that you were appointed receiver: Tell how you happened to be appointed receiver and when you got that information.

A. Well, I was appointed receiver by Judge McNary. I had no previous business connected with the Western Bond and Mortgage Company. In fact, I knew nothing about its affairs; had paid no attention to it as a corporation; and the first notice I had of it was the Judge called me on the phone and told me he had appointed me receiver

(Testimony of George M. McBride.)

of the Western Bond and Mortgage Company and, shortly after that, on the same day, Mr. Moody came to my office and also told me that I had been appointed.

Q. You made no effort to be appointed, did you, or was that the first——

A. I had made no effort to be appointed to that job whatever.

Q. And you had no information of it until, as I understand, you were given that information by Mr. Moody, that the Judge had appointed you, is that right?      A. Yes.

The Court: Just a moment. That is inconsistent. He has just already said that the Judge called him first, as I understand it. Is that correct?

The Witness: The Judge called me and said he had appointed me. [4]

The Court: That was before you talked to Mr. Moody?

The Witness: Yes, Mr. Moody talked to me just a little while later, a little while afterwards. He came from the court, as I recollect it, down to my office and told me.

The Court: I do not think it is material, but you let him answer the other way.

Mr. Teiser: I misunderstood.

Q. How long did you act as receiver?

A. From the date of my appointment, August 13, until, I think, about the 12th of December.

(Testimony of George M. McBride.)

Q. What happened on the 12th of December that caused you to cease acting as receiver?

A. Well, I was appointed as Trustee in Bankruptcy.

Q. What did you do as receiver? During this period between August 13 and December 12, what did you do as receiver?

A. Well, I looked at the property, what I could find. I was largely familiarizing myself with the property and with the contents of the office and the books, that is, the regular books of the Western Bond.

Q. I may ask you: when did you first get any information of the facts or the claims set forth in your action in this court in this present action, Civil Case No. 2202? When did you first have any intimation of the facts set forth in your complaint?

A. Well, I believe about July or August, 1943.

Q. How do you fix that date in your mind? Did anything occur at that time that fixes that date in your mind?

A. Well, we were looking up the facts relative to the claims of the Income Tax Department along in the summer and we had—had employed Mr. Erickson as accountant to go into the matters relative to that claim and make an exhaustive accounting of the facts so that we might know how to meet the claim of the Government as to income tax.

Q. Do you remember offhand how much it was,

(Testimony of George M. McBride.)

roughly, in round numbers? How much was the claim of the Government?

A. The claim of the Government was originally about \$51,000 and there was accrued interest by reason of the running of the claim.

Q. What did you do in regard to assisting Mr. Erickson in ascertaining the facts in regard to these tax matters?

A. We employed Mr. Erickson under orders of the Referee to go into the matter, and he had been given access to the books and told to make an exhaustive search.

Q. What came to us about that time, if anything?

Mr. Reilly: Who do you mean by "us"?

Mr. Teiser: The Trustee. I am talking about the attorney and Trustee.

Mr. Reilly: I object to his testifying about anything that came to anyone excepting he himself.

Mr. Teiser: All right. [6]

Q. What information did you get, and from what source did you get it, in aid of Mr. Erickson?

A. Well, Mr. Erickson, in going over the matters of the income tax, had found facts which—

Mr. Reilly: Just a moment, if the Court please. I object to the statement as to what Mr. Erickson found, as hearsay.

The Court: Just testify to what you know.

Q. Just tell what information you obtained and where you obtained it from, if you obtained any-

(Testimony of George M. McBride.)

thing in regard to determining the situation as to income tax.

A. Well, what I obtained was facts relative to the income tax matters, which showed me or at least——

Q. Just a minute. Did you obtain any document from anybody or any report from anyone at that time in connection with this matter?

A. Well, we had a report, of course we got a report from the income tax people, from the revenue agents.

Q. That is what I was trying to find out.

A. And that report, of course, was a report that they—they had made an investigation back in 1930. I had never seen that report up to that time.

Q. Then, you did get a report?

Mr. Teiser: Have you got those statements?

Mr. Reilly: No, Mr. Parker is out there checking them for you. [7]

Mr. Treiser: If your Honor please, there is a pre-trial exhibit, which is the report that he refers to, that I would like to introduce, or have him identify it, but these documents are in the Clerk's office. We had withdrawn the exhibits and I turned them over to Mr. Reilly, and Mr. Reilly's assistant is back there checking them off.

Mr. Reilly: I think there was probably a misunderstanding between us. Mr. Teiser took the exhibits out, receipting for them, and then turned them over to me. He understood I was to check them. The result is, they were not checked and we



(Testimony of George M. McBride.)

are having them checked with the Clerk at this moment. I think they ought to be checked now. May I be excused to run in there?

The Court: Take a recess and let us get the case ready for trial.

Mr. Teiser: I am sure we are ready for trial, your Honor.

The Court: I do not know anything about that. This has gone through to a pre-trial order, and that is what a pre-trial order is for, to get these documents in shape so they can be introduced without any delay. Here, it is not done, so the Court will take a recess.

(Recess.)

Q. Mr. McBride, will you look at the paper I am now handing you, through the courtesy of the bailiff, plaintiff's Pre-Trial Exhibit No. 59, and state whether that is a copy of the revenue [8] agent's report that you have stated you received sometime around June, 1943?

A. Yes, that is the copy of the revenue agent's report.

Q. Is that the one you received, sir?

A. Yes.

Mr. Teiser: I ask that that be marked as plaintiff's—shall we keep the same numbers, your Honor?

The Court: Yes.

Mr. Teiser: I ask that that be marked as plaintiff's exhibit 59, or is it 69?

Mr. Reilly: 59. The defendant objects to the

(Testimony of George M. McBride.)

introduction in evidence of this exhibit, insofar as it is offered as proving or tending to prove any of the statements therein contained, or for any purpose, except the limited purpose of explaining or tending to explain the excuse offered by the plaintiff for having delayed the bringing of the action so long. For that purpose I consider it material, but not for any other purpose.

The Court: Admitted.

Mr. Reilly: For which purpose, your Honor?

The Court: Well, what use I will make of it after it gets in evidence, I do not know. I cannot try to exclude other matters from my mind, so I am going to admit it. Take what exceptions you feel you should, but I cannot read a document for a special purpose, as far as I know.

Mr. Reilly: I think with the statement the Court makes that we should object to admitting the document at all, on the [9] ground that it is an unsworn statement made by a third person, outside the knowledge of this witness.

The Court: The document is admitted, and the Court is not going to pass any judgment on hearsay, as you well know, but it is admitted for all competent purposes.

(Copy of letter dated May 27, 1943 from Treasury Department, Washington, D. C., to Collector of Internal Revenue, Portland, Oregon, heretofore marked plaintiff's Pre-Trial Exhibit No. 59, was thereupon received in evidence and marked Plaintiff's Exhibit No. 59.)

(Testimony of George M. McBride.)

Q. Why was it you did not happen to get that, or a copy of that report, or see a copy of that report previous to the time you did receive it, and how was it you happened to receive it then?

A. They filed their claim sometime in 1935.

Q. Who is "they"?

A. The revenue agent of the Income Tax Department.

Q. United States Government?

A. Yes. They filed their claim sometime in 1935. At that time, or shortly after the filing of the claim, I went up to Mr. Cannon's office, who was then Referee, with this and we discussed the matter of making objections to the claim at that time.

Q. That is, the Government's lien? [10]

A. Yes, but Mr. Cannon——

Mr. Reilly: Just a moment, please. The defendant objects to any conversation between the witness and Mr. Cannon, or any instructions from Mr. Cannon, because, first, it is hearsay and, secondly, it would afford no excuse for any failure on his part to perform his duties as Trustee.

The Court: Well, I have to find out why he did not take action before 1943. The only way I can find that out is to listen to what he did. If he got information from somebody else that prevented him from finding out, still that would be competent if he did not find out. You may proceed.

Mr. Reilly: Exception, your Honor?

The Court: Yes.

(Testimony of George M. McBride.)

A. Mr. Cannon, as Referee, stated that we had no money at that time.

Q. Pardon me. Did you say what we attempted to do when we went up to Mr. Cannon's office? Did you say what was attempted to be done by us when we went up there? What was our purpose in going there?

A. We went up there for the purpose of contesting the Government's claim. Mr. Cannon stated that there was no reason at that time to contest the claim, for we had no money to pay any claim at that time and it was merely—would be merely a gesture, and he considered it better to put the matter off until we had something to pay a claim with, as the whole matter [11] would probably have to be threshed out later on, so he did not allow the filing of a contest at that time.

Q. Were those his instructions to you?

A. That was his instructions to me.

Q. And when did you file a contest or objections to the claim of the Government? A. In 1943.

Q. How was that time measured in regard to the time when you had money with which to do it, to pay it or pay any substantial part of it?

A. I do not understand the question.

Q. I say: you say that you filed objections to the claim of the Government in 1943?

A. Yes.

Q. I ask you, then, when you filed objections to the claim in 1943, what relation did that time have

(Testimony of George M. McBride.)

as to whether you had any money in the estate to pay the claim?

A. We had received a large amount of money, approximately \$94,500, from the Bank of California in our suit against the bank, and the Government, knowing that we had——

Q. When was that? What year was that that you received that money?

A. Well, we received that money—that was early in—sometime early in 1943 or sometime in 1943, I cannot remember the exact date. [12]

Q. After you received that money, did you then file, as I understand, an objection to the claim of the Federal Government for taxes?

A. We did file an objection after we had investigated it, had an accountant investigate the matter, we filed our objection to the Government's claim.

Q. When did you start that investigation on which to base the filing of objections, compared to the time you received this money from the Bank of California?

A. Well, it was a few months. I could not say just how long, but it was within, anyway, five or six months, I would think. My recollection is a little hazy as to the exact time.

Q. Was it around the time that you received this money that you began investigating as to filing objections to the claim of the Government for taxes? A. Yes, it was shortly afterwards.

Q. What did you do then in regard to formulating your objections as to the Government's claim

(Testimony of George M. McBride.)

at that time, in addition to getting this report from the revenue agent that you have just testified to? I think you have already testified to some of it, Mr. McBride. Maybe that is why you are puzzled. I think you have stated what you did previously, but I am asking you again so as to get the sequence of time.

A. Well, we filed a contest against the Government's claim before the Court—before the Referee. [13]

Q. What information did you have and how did you get the information on which to base the filing of that claim?

A. Well, we had, as I stated before, hired Mr. Erickson to make an exhaustive search of the records.

Q. Who is Mr. Erickson? What position did Mr. Erickson hold? What is his business?

A. He is an auditor and accountant, a certified public accountant.

Q. Did you or did you not give Mr. Erickson this revenue agent's report? A. Yes.

Q. In connection with this?

A. Gave him the report.

Q. When did Mr. Erickson report to you? About what time did he make a report to you of his examination?

A. It was along about the latter part of July, if my recollection serves me.

Q. What did he report to you in connection



(Testimony of George M. McBride.)

with the matters which you have set forth in your complaint as claims 1 and 2?

Mr. Reilly: That is objected to as hearsay.

Mr. Teiser: Pardon me. I think you are right. I will withdraw my question.

Q. Did or did he not give you the first—was or was not the first information conveyed to you in regard to those claims as set forth in your cause of action given to you by Mr. [14] Erickson?

A. Yes.

Q. What did you do when he informed you of the facts set forth which caused you to bring this action? What did you do before bringing the action, if anything, or what was done on your behalf?

A. Well, I had Mr. Erickson make an exhaustive audit of such books as appeared to him necessary to establish the action if the facts appeared to warrant it.

Q. Was any examination made of any parties, in court or otherwise, pursuant to the discovery of information by you?

A. Yes.

Q. Could you state just the nature of this examination, or what it was?

Mr. Reilly: That is objected to as calling for a conclusion of the witness. He may state the name—

Mr. Teiser: That is what I mean, just the character of the examination.

Q. Was it in court? Was it a deposition, or just what was it?

(Testimony of George M. McBride.)

A. Well, it was before the Bankruptcy Court in the matter of bringing the facts out.

Q. How soon after you discovered this information from Mr. Erickson and had the examination conducted in the Bankruptcy Court did you bring this action?

A. Well, it was in, I think, about a month or two at the most. [15]

Q. Did you inspect the books and records of the Western Bond and Mortgage Company in 1934, or any time thereafter, you, yourself?

A. I inspected some of the books. We had probably three or four tons of records altogether in the files down in the basement, but the main books of the Western Bond and Mortgage Company I inspected.

Q. From such inspection, did you get any information of the situation set forth in your complaint? A. No, I did not.

Q. Had you any information from any source, previous to that obtained from the revenue agent's report, and from your certified public accountant, and from the examination in the Bankruptcy Court? Had you obtained any information from any source other than that? A. No.

Q. Or earlier than that? A. No.

Q. In regard to this suit? A. No.

Q. Did you? A. I had not, no.

Mr. Teiser: I think that is all.

(Testimony of George M. McBride.)

Cross Examination

By Mr. Reilly: [16]

Q. How old are you, Mr. McBride?

A. What is that?

Q. How old are you? A. Sixty-eight.

Q. How long have you lived in Oregon?

A. About sixty-six years altogether.

Q. Do those sixty-six years include from about 1900 to date? From 1900 to date? A. Yes.

Q. How long have you lived in the City of Portland? A. About thirty-six years.

Q. Continuously to date? A. Yes.

Q. In other words, I mean your residence has been constant? A. Yes.

Q. For the last thirty-six years or so?

A. Yes.

Q. What was your occupation in the 1920's?

A. Well, I was in the Internal Revenue office during the latter '20's, from 1923.

Q. Until when? A. Until 1933.

Q. 1923 to 1933? A. Yes.

Q. What were you doing in the Internal Revenue office? [17]

A. Well, I was chief of the division of the estate tax department for quite some time, part of that time, and I was chief of division of the income tax department for the last five or six years.

Q. Then, for the last five or six years preceding 1933 you were chief of the income tax division of the United States Internal Revenue office at Portland? A. Yes.

(Testimony of George M. McBride.)

Q. That, I assume, necessarily involved a considerable knowledge of accounting?

A. Yes. It involved some knowledge of accounting, enough to read a balance sheet and to know the revenue laws.

Q. And enough so that you could understand a set of books?

A. Well, it was enough so I could understand some books, but I was not at all to be rated with a certified public accountant.

Q. However, you were acquainted with the revenue laws; you knew that a claim had be to presented within a certain time, and that an objection to a tax had to be presented within a certain time after notice of the tax was levied?

Mr. Teiser: I object to that. It is not a correct statement of the law and I do not see——

The Court: Overruled.

Q. During the time that you were chief of the income tax division here in Portland, did you have to do with the claim of the Government against the defendant herein for taxes for [18] the year 1929, where the Government undertook to collect, for Western Bond transactions some \$150,000?

A. No. I had nothing to do with that end of it at all. That was all handled by the revenue agent's department, from the Commission's office in Washington. We had nothing to do with that part of it.

Q. You knew of the fact of the claim?

A. No, I did not know of the facts of the claim. I just had what you might call a gossip knowledge

(Testimony of George M. McBride.)

of it, but I had nothing to do with the facts of the claim directly.

Q. The subject of the possible liability of Mr. Farrington for income tax was considerably gossiped about in your office?

A. Well, yes, some of it may have been.

Q. Some of the members of your office later offered testimony in the case before the Board of Tax Appeals?

Mr. Teiser: What time are you speaking about, Mr. Reilly?

The Witness: I do not recollect any such thing.

The Court: Let the witness answer. Don't you try to answer for him.

The Witness: I did not know of any such thing.

Q. But you knew, in any event, the Government, prior to 1934, was making a claim against Mr. Farrington, charging him with fraud in some of his Western Bond transactions, fraud on the Government?

A. The only knowledge I had was an occasion of some kind when [19] Mr. Farrington got the books, some of the Western Bond books, from me, and there was an action either against Mr. Farrington or Mr. Ridgway, I am not certain which, and I gave them the books, but kept custody of them until we got up to the court house and until they had been introduced in evidence or at least taken charge of by the Court. During that time, I sat there and listened to some of the testimony for awhile and then went back.

(Testimony of George M. McBride.)

Q. That period of time you are talking about is the time they had the trial before the examiner of the Board of Tax Appeals, is that right?

A. This wasn't anything, so far as I know, relative to—it was not anything to do with this 1930 matter of the Western Bond and Mortgage Company. In fact, I don't know what all the facts were because I had nothing to do with it.

Q. But the time when this occurred and you sat and listened to the testimony, and brought the books up, was when the case was tried before the examiner of the Board of Tax Appeals here in this building, in Portland? A. Yes.

Q. How long did you sit and listen to the testimony in that matter?

A. Oh, I don't remember exactly, probably an hour or two. I listened to them testifying on the stand. I think Mr. Ridgway was testifying when I was there but I don't know what—it did [20] not involve anything which concerned me and the Western Bond and Mortgage Company, particularly, in my end of it.

Q. It was Mr. Farrington's tax case, was it?

A. I would not say whether it was Mr. Farrington's or Mr. Ridgway's.

Q. During 1931, did you take a daily newspaper? A. Yes.

Q. Which one, or did you take both the Oregonian and the Journal?

A. I could not tell you which one I was taking at that time, because at different times I took dif-



(Testimony of George M. McBride.)

ferent papers, depending on how well they could be delivered to my home which was out in Multnomah at that time. I would not know.

Q. You read the papers, whichever one you took?

A. Well, I read parts of them. I won't say that I read all of them by any means, or all of any paper.

Q. Are you able to recall now having read anything about the Western Bond and Mortgage Company in the newspapers in 1931?

A. No. If there was anything in the newspapers, it was not brought to my attention. There was nothing there that I noticed about it particularly.

Q. You never had seen any newspaper articles during 1931 about the Western Bond and Mortgage Company? I mean, you have not seen any such papers since they were printed?

A. No, I have not.

Q. Not up to the present date? [21]

A. Well, I won't say up to the present date because one or two of these articles that were in there which concerned me personally, since I was trustee, I noticed some of them.

Q. I am talking about the 1931 newspapers.

A. No, I do not remember having seen anything in the newspapers back at that time at all.

Q. Mr. Teiser, your attorney, did not ever show you anything in any newspapers?

A. Not that I remember of.

Q. Did you attend the taking of the deposition

(Testimony of George M. McBride.)

of Mr. Brown, Brown's deposition, when you were taking the depositions of a man named Brown and Dr. Besson in the Bankruptcy Court where articles from the Oregonian in 1931 were displayed by your attorney?

Mr. Teiser: If your Honor please, I submit the question is not quite fair, unless you say what papers were submitted, what newspapers were handed him, because, as a matter of fact, the newspaper article handed him was a newspaper record of the bankruptcy and nothing else.

The Court: Well, he can ask. If the witness does not know, it is perfectly permissible for him to say that he does not know.

The Witness: Will you ask the question again?

Q. Did you attend that deposition, those depositions of Brown and Besson? [22]

A. I think I was present. I won't even be sure of that, but I believe I was present when they made their depositions.

Q. Do you recall Mr. Teiser showing to those witnesses newspaper clippings concerning the troubles of the Western Bond and Mortgage Company back in 1931?

A. No, I do not recall it now.

Q. All right. Your connection with the income tax department terminated, when, in 1933?

A. Terminated about July.

Q. July, 1933? A. July, 1933?

Q. How long had you been there? Since 1923?

A. Yes.

(Testimony of George M. McBride.)

Q. During that ten years, that had been your exclusive occupation? A. Yes.

Q. Then, in 1933, that job, you being a Republican, kind of faded away from you, is that it?

A. It did.

Q. You then went out and undertook to practice law, or what did you do?

A. Well, I practiced law when I could find any to practice.

Q. And I wonder if you did not, yourself, approach Judge McNary to ask whether there was anything that the court could find for you in the way of receiverships or something of that [23] sort?

A. Yes.

Q. That was prior to your appointment as receiver of this corporation?

A. Yes, some time before that. I just, as a matter of conversation—as a conversational matter; I asked if there was anything of that kind, I would be very pleased to handle it.

Q. You needed the work? A. Yes, I did.

Q. During that year that you practiced law, before you became receiver of the Western Bond and Mortgage Company, did you hold yourself out to the public as an income tax expert?

A. As an income tax counsellor. I never said "income tax expert."

Q. Well, in July of 1934, you needed the job, when you got the job as receiver of Western Bond, did you?

A. Well, I needed any job that came along in

(Testimony of George M. McBride.)

connection with my law work which would be lucrative.

Q. Then, on the 20th of July, you were appointed receiver of the Western Bond?

A. On the 13th, to be exact, I believe, the 13th of August?

Q. Oh yes. I had the wrong date. The 13th of August?

A. The 13th of August.

Q. August 13, 1934, you were appointed receiver of the corporation? [24]

A. Yes.

Q. And at that time the corporation was under investigation by the Attorney General's office and the Corporation Department, was it?

A. Yes. I did not know it at that time, however, because it had not been brought to my attention.

Q. That investigation was being conducted on behalf of the Attorney General by Ralph E. Moody?

A. Yes.

Q. And on behalf of the Corporation Commissioner by some auditors?

A. Yes.

Q. Immediately after your appointment as receiver, you were waited upon by Mr. Moody?

A. Yes.

Q. And he discussed with you, at considerable length, the affairs of the Western Bond and Mortgage Company, did he not?

A. Yes.

Q. And he discussed with you at that time the possibility of a suit against Mr. Farrington, isn't that a fact?

A. I won't be sure what he discussed or what

(Testimony of George M. McBride.)

particular suits we discussed. We discussed matters in general, but we did not have any particular case in point, so far as I remember, at all.

Q. Did he discuss with you at that time the old litigation which had been pending in 1931? [25]

A. Not that I remember at all.

Q. Would you say that he did not?

A. Well——

Mr. Teiser: Which case in 1931 do you mean, Mr. Reilly?

Mr. Reilly: Well, there were half a dozen cases.

Q. Brockie against Western Bond and Mortgage Company and Mr. Farrington and others; Thompson and some dozen or so others against the Western Bond and Mortgage Company, in which Mr. Farrington was named as a defendant—he was not named as a defendant but his name figured prominently. Then there was the King—I think there was another one. That is not the name.

Mr. Teiser: Pape.

Q. Pape and others, and then there was some other case referred to in the affidavit of Mr. McCurtain, all having to do with alleged defalcations by officers of the Western Bond and Mortgage Company, and most of them having Mr. Farrington's name mentioned.

Was any of that litigation discussed at all?

A. Not in the way of any particular thing, as I remember it. I had heard so many things said about Mr. Farrington and Mr. Ridgway by different



(Testimony of George M. McBride.)

ones who had lost their money, and all of those things got to be such a jumbled mass in my mind, from what things were brought to my ears, that the only thing I could do was to try and separate what seemed to be gossip [26] from something which was a fact.

Q. This gossip started coming to you at once upon your appointment as receiver, did it?

A. No, I don't think there was anything brought to my notice which would in any way affect this suit which we have brought at this time.

Q. The gossip about Mr. Farrington that you referred to a minute ago, that started coming to your ears very shortly after your appointment as receiver, did it not?

A. I don't know which particular thing about Mr. Farrington that you are referring to.

Q. I am referring to the things that you referred to a minute ago, the gossip there about Mr. Farrington, and you also included Mr. Ridgway—we will leave him out of this picture—the gossip about Mr. Farrington from investors or stockholders or people who had lost money in the Western Bond and Mortgage Company. That is what I am referring to. When did that start coming to you?

A. Well, those things were referred to by people who had lost money, who were sore about losing their money, but there was nothing so tangible about any of it that would put me on any notice as to any particular thing which they were referring to.



(Testimony of George M. McBride.)

Q. When did this sort of thing start, how soon after you were appointed receiver?

A. Well, the bondholders were coming in there, from eight or [27] ten in a day, many times.

Q. Beginning, when?

A. Beginning shortly after my appointment as receiver.

Q. When you say "shortly after" you mean within, at the outside, a month or two?

A. Oh well——

Q. Less than that?

A. Less than that, I would say.

Q. Within a week they started to come there?

A. Well, I would not say exactly because I did not keep any track of it.

Q. And they were very numerous, these people who came in and made complaints?

A. Yes they were very numerous. The people that came in, they were wanting principally to know when they were going to get their money.

Q. A good many of them were making charges against Mr. Farrington of one sort or another?

A. Well, as I say, very little of it was tangible.

Q. But, nevertheless, they were saying to you that Mr. Farrington had defrauded them, even though it was not tangible?

A. Well, they mentioned him along with Mr. Ridgway and Mr.——

Q. O'Flynn?

A. Mr. O'Flynn, who was the latter man in there. Mr. O'Flynn got the worst of the panning

(Testimony of George M. McBride.)

from the bondholders, but Mr. [28] Farrington and Mr. Ridgway, and some of the salesmen, as well, came in for panning by the people who had bought the bonds and were not able to cash in on them, so they were all sore about it, so there was conversation, naturally, sometimes along that line.

Q. What, if any, effort did you make while you were receiver to investigate any of these complaints?

A. Well, I looked up all of the tangible things that I could on the books of the Western Bond and Mortgage Company.

Q. What does that mean? Does that mean you examined the books?

A. Yes, I examined some of the books. I probably did not examine all of them. There was a very intricate system of bookkeeping and a great many subsidiary corporations and I, coming in without any knowledge of their bookkeeping system or anything of that kind—it was rather confusing to me. I had no way to go into anything very intricate about the——

Q. At the time Mr. Moody discussed this matter with you, he tendered you the aid of the auditors of the Corporation Department, did he not?

A. Well, to a limited degree. They were willing to explain anything to me that they could. Mr. Brown and Mr. Goodwin, I believe, had made an audit of the books, and up to that point they could have explained some things which I was unfamiliar with.

(Testimony of George M. McBride.)

Q. And Mr. Moody offered the services of these two auditors for the purpose of making any further investigation you wanted [29] made?

A. Yes.

Q. And at that time you were placed on a salary from the Corporation Department, was it?

A. No.

Q. The Attorney General's office?

A. The Attorney General.

Q. The Attorney General's office? A. Yes.

Q. The Attorney General put you on a salary of \$150 a month and paid your office expense, is that right?

A. Well, yes, they paid the expenses of the office there and this salary, if you can call it a salary, was to cover what investigations I could make as to what the thing was all about, in addition to what the auditors had found.

They told me that they had to make a rather quick audit of the thing and there might be other things which they had not found, but anything that came to my notice, they would be glad, naturally, to know about.

Q. An investigation for you?

A. Well, the investigation at that time was largely on Mr. O'Flynn's actions. We had not gone back of that particularly because the books that they were using at that time were largely books that had been in there through Mr. O'Flynn's term as an officer, so we did not go back of them very

(Testimony of George M. McBride.)

much. In fact, I [30] could not, because I did not know enough about the books.

Q. Mr. McBride, at the same time, the District Attorney was investigating the Western Bond and Mortgage Company, was he not?

A. Not that I know anything about. I never had—If he had anybody doing anything about it, I never saw them.

Q. You never discussed this matter with the District Attorney? A. No, I did not.

Q. During 1934 you were taking one or the other of the newspapers? A. Yes.

Q. And, of course, anything at or about the time of your appointment or thereafter, that related to the Western Bond and Mortgage Company, you read with considerable interest?

A. Well, yes, if I saw it. I might have overlooked some of the things, but I would not be sure about it.

Q. Do you know which paper you took at that time? A. No sir, I would not remember.

Q. I hand you herewith defendant's Pre-Trial Exhibit 79, being an article from the Oregonian of July 20, 1934, and I call your attention—you may read the whole thing, of course, but for the sake of what I want to ask you about, I call your attention to the last paragraph on the second page of that newspaper article appearing in the Oregonian of that date.

A. The next to the last paragraph?

Q. No, the last paragraph. Having refreshed

(Testimony of George M. McBride.)

your memory from that newspaper article, particularly that paragraph, I will ask [31] you if you now cannot recall that Mr. Moody and you discussed the question of both the civil and criminal liability of Mr. Farrington in connection with transactions while he was an officer of the Western Bond and Mortgage Company?

A. I do not remember any specific instances. We discussed the liability of most everybody who was connected with the matter, in a general way.

Q. Never mind anybody else. Let us confine this to Mr. Farrington. With that paragraph before you to refresh your memory as to what was said and done at that time, can't you now recall that you and Mr. Moody did discuss both the civil and criminal liability, if any, of Mr. Farrington for matters arising during his presidency of the Western Bond and Mortgage Company?

A. I cannot remember any specific instance. We maybe did so. This has been ten years ago and I cannot remember it specifically.

Q. Have you read these exhibits?

A. Not lately, no. If I have ever read them, I don't remember.

Q. Have you read them at all?

A. I would not even know, excepting your telling me that this is a copy of an article in the Oregonian. I would not remember back far enough to remember any article in the Oregonian ten years ago. I could not remember the article or whether I saw the article at that time. [32]



(Testimony of George M. McBride.)

Q. Well, it has been stipulated that these are articles in the papers——

Mr. Teiser: What date was that?

Mr. Reilly: This was July 20, 1934.

Mr. Teiser: It was before he was appointed?

Mr. Reilly: Yes.

Q. I will show you some later ones. I think you had better look this one over, Mr. McBride, and I will let you pick between them. The bailiff will hand you defendant's Pre-Trial Exhibit 78, along with it, which is an article from the Journal, and you pick out the paper that you were taking at that time. I want you to look those articles over and presently I want to offer them in evidence.

Mr. Teiser: What date is that article?

Mr. Reilly: On that same date, or the day before or the day after.

Q. Which one do you think was in the paper you took?

A. Well, even now, I would not be certain at that time what paper. I took the Journal part of the time, and, a part of the time, I took the Oregonian. To remember back ten years as to what paper I read at that time or what I saw, I could not testify because I would not know.

Q. The articles are substantially alike. You read one or the other at that time?

A. Well, I could only say that I read one or the other of those [33] papers. What I read there I would not be able to testify to, of course, any



(Testimony of George M. McBride.)

more than you would be able to testify what paper you read ten years ago and what you read in it.

Q. Well, at that time, you were considerably interested in Mr. Farrington because of the gossip that had been around the income tax department about his supposed or alleged tax liability, isn't that right?

A. Well, I was interested at this time because, naturally, as an officer of the Western Bond, why, his name was mentioned quite often with relation to it.

Mr. Reilly: We will offer defendant's Pre-Trial Exhibits 78 and 79 in evidence, your Honor.

Mr. Teiser: If you Honor please, I do not know of any statement that he made which indicates that they would be evidentiary in any way.

The Court: Objection?

Mr. Reilly: It is stipulated that they were in the public press on the date indicated.

Mr. Teiser: No question about that.

Mr. Reilly: Prominently displayed there for all men to read.

Mr. Teiser: No question about the fact that they were in the public press.

The Court: We can do this two ways. We can admit all of these matters, or we can leave them until the time they are properly admissible. I take it that you probably would have [34] some testimony that you could put on that would make them properly admissible. As far as this date is concerned, he does not even remember about it.

(Testimony of George M. McBride.)

Mr. Reilly: They are pre-trial exhibits.

The Court: Yes.

Mr. Teiser: I will admit, if your Honor please, that those two articles appeared in the papers which they purport to appear in, at the time set forth on those articles as having appeared.

The Court: I will follow my usual rule. The documents are not admissible on cross examination.

Mr. Reilly: Very well, your Honor.

The Court: Unless they are stipulated in.

Q. Mr. McBride, how long did you continue as receiver? A. What is that?

Q. How long did you continue as receiver?

A. Until, I believe, the 12th of December when I qualified as the Trustee.

Q. 1934? A. 1934, yes.

Q. In the meantime, the corporation had been adjudicated a bankrupt? A. Yes.

Q. During all the time that you were receiver the Attorney General paid you your salary of \$150 a month and your office expenses? [35]

A. Yes.

Q. What services were performed for the Attorney General's office except that of investigating the things that had been discussed with you about Mr. Farrington and the other officers, with an eye to criminal prosecution?

A. Well, I was investigating whatever came under my notice relative to either criminal or any proceeding which would help the bondholders.

(Testimony of George M. McBride.)

That was merely to help out in a general way and as to what had gone on.

Q. During the fall of 1934, I will ask you whether or not the office of the Attorney General of Oregon communicated, to your knowledge, with all of the creditors and stockholders of the Western Bond and Mortgage Company, by mail?

A. I found out after this matter had happened that they had, but I did not know at the time, and before he did communicate with these bondholders, that he had done so.

Q. I will ask you whether or not in these communications the Attorney General solicited powers of attorney and advised claimants that it was the intention of the Attorney General to vote all proxies received for you as Trustee of the bankrupt estate?

Mr. Teiser: I object to that as immaterial, irrelevant and incompetent respecting any issue here on trial; also, I submit whether the Attorney General——

The Court: The objection is overruled. [36]

A. I could not state exactly what the Attorney General's office did do. It would be something that Mr. Moody could tell you about much better, because I did not take any particular notice of that. However, all of these claims—not all of them, but a great many of them were made out, giving a power of attorney to the Attorney General, so I would suppose that that probably happened.

(Testimony of George M. McBride.)

Q. A great mass of claims were put through the Attorney General, were they not?

A. Yes, a great many of them.

Q. And it was by the vote of the Attorney General under those proxies that you were elected Trustee?

A. Yes, I think that at least was quite—really was one of the things that helped to make my election certain.

Q. Well, as a matter of fact, did not the Attorney General have very much more than a majority of all claims?

A. I never went into that particularly to know how many of them he had. I know I was elected Trustee and, up to that time, I had not taken any particular interest in it as to just how the matter was progressing. I knew that the notices had been sent out, and I know that I was elected Trustee, but as to these other things, as to who the Attorney General sent these notices to, I really was not interested.

Q. Did you continue, after your election as Trustee, on a salary from the Attorney General's office? [37]

A. Up to around, as I recollect, the first of June.

Q. Of 1935?           A. Yes.

Q. A salary of \$150 a month?

A. \$150 a month, yes.

Q. And for what purpose?

A. Well, the same purpose that had been before,

(Testimony of George M. McBride.)

investigating ordinarily into the various things that came before me and investigating also about seven or eight hundred claims, which came into the Bankruptcy Court and which were sent down to me at the office in the Western Bond, the old building there where they had the office, and which claims, it was necessary for me to go over and get them into some shape to refer to them as the various claimants wrote about them or were later, perhaps, to get a dividend on.

Q. Mr. McBride, that was a part of your duties as Trustee. What were you doing for the Attorney General?

A. Well, now, that would be listed as investigations, and I gave them whatever I thought would help in any way or would be a help to the bondholders and to the Attorney General in any criminal investigation that he was making.

Q. During the time that you were Trustee and were also receiving a salary from the Attorney General's office, did you devote your whole time to the Western Bond and Mortgage Company affairs? [38]

A. Well, not altogether. There were a few cases which came to me, which I was able to handle, but it was necessary finally to give up my office in the Failing Building because I was called to the other office so many times I could not carry on both offices at the same time, and it was necessary to devote practically the whole time to that for the first year.

(Testimony of George M. McBride.)

Q. When did you move down to the Western Bond office?

A. Oh, well, I went down there the morning that the Judges approved the bond. I went immediately down there and I spent more than half of my time there from then on. I never was able, after I began to go into matters, to spend more than half of the time in my own office.

Q. When did you actually move down to the Western Bond building?

A. I could not tell you when I gave up the other offices, but there was not any particular necessity for keeping them, because there was nothing to justify it.

Q. In 1935, as I understand it, you were apprised of a claim made by the Internal Revenue Department against the corporation for taxes?

A. Yes.

Q. And in what form was that claim made? In writing?

A. Well, originally there was an assessment, what they termed, I think, an emergency assessment. They sent a copy of that to the Western Bond and Mortgage Company, and, later, they filed this claim, which is a routine claim that they file, against [39] all additional taxes that are assessed and have not been paid. They filed that claim to protect the Government against any conveyance of property or anything which might result to its detriment.

Q. You, as a former head of the Income Tax



(Testimony of George M. McBride.)

Department in Portland, and as a tax counsellor for the year after your retirement, knew perfectly well how to get information as to the basis of that claim, did you not?

A. No, I did not. I did not have any copy of the revenue agent's report at all and I never did get one until this matter came out here.

Q. What effort did you make to get the information concerning that tax claim?

A. Well, I went up to the revenue agent's office to see if they had a copy or could get me a copy of that, and they did not have any copies, and they said they wrote to the revenue agent in charge at Seattle and he did not have a copy that I could have. Some long time later—I do not know just how long—they told me—I went up later on and they said that they thought that Mr. Jacobs had a copy; that he had been handling the matter at that time. I went up to his office later, quite some time later.

Q. What do you mean by "quite some time later"?

A. Oh, it was several—I would say three or four years later.

Q. Three or four years? [40]

A. Some time anyway. Mr. Jacobs was away. He was in the east and I did not—the girl did not know anything about it and, so, I did not get it.

Q. And you did not go back there?

A. I did not go back. I thought that when the time came that the claim came up that we would

(Testimony of George M. McBride.)

get a copy of it from the Attorney General or somewhere, and there was not any particular necessity in the meantime, because it had to come up later anyway.

Q. Then, as I understand you, the extent of your efforts to ascertain the basis of this claim of the Government for \$50,000 was one visit to the office of the Internal Revenue Department in Portland and one visit to Bob Jacobs' office, on which occasion you found him to be out of town?

A. Yes. I do not remember any other times that I went after that. It was not coming up at that particular time, and the assessment that was made explained it enough to know how much they claimed, and there did not seem any necessity for going into it so much deeper until the claim was acted on before the Referee, so I did not go any further with it when I found that Mr. Jacobs was not there, and I did not know he even had it.

Q. In March of 1935, you, with the consent of the Referee in Bankruptcy, employed an attorney to assist you in your work as Trustee and in your investigations? [41]

A. I employed an attorney to do anything that was necessary for an attorney to do to take action before the Referee in Bankruptcy and before the court.

Q. That attorney was John R. Latourette of Portland?      A. Yes.

Q. I will ask you whether John R. Latourette did not discuss with you, in considerable detail, the

(Testimony of George M. McBride.)

advisability of undertaking to bring an action against Mr. Farrington on any of the things which had been mentioned in the 1931 lawsuit?

A. I don't remember having discussed that with Mr. Latourette at all.

Mr. Teiser: What lawsuit?

Mr. Reilly: The 1931 lawsuit.

Q. At the time you employed Mr. Latourette, you still had available the services of the auditors of the Corporation Commission?

A. As I say, the availability of those services was very limited. They were willing to tell me anything that they knew, that they had learned on the audit, but they were working on other cases for the Corporation Commissioner, and, they did not, so far as I judged from their actions—they merely wanted to get such advice and assistance as they could without taking up the time——

Q. Who put a limit on their activities in your behalf?

A. I would not know about that, about how they were limited, as [42] to the Corporation Commissioner.

Q. Did anybody suggest that they had any limitations put on their activities?

A. Not specifically, no.

Q. Did you ever ask the Attorney General for instructions to them to give you assistance?

A. They were in the office with Mr. Moody at different times, but I do not believe—they never stated to me that they had instructions to go on

(Testimony of George M. McBride.)

any specific audit, just simply to give such help as they could with reference to the thing, having knowledge by reason of having made an audit of the Western Bond.

Q. Did Mr. Moody, when he was there with the auditors, ever place any limitation at all upon their activities, or did he offer you free reign?

A. I could not say as to that. He did not make any specific statement to that effect, as far as I know.

Q. You, yourself, with the approval of the court, employed an auditor on a contingent fee basis in 1936, did you not?      A. In 1936?

Q. Correct.

A. Well, I employed an auditor in 1936, through the order of the Referee.

Q. That was Mr. R. Erickson?      A. Yes.

Q. And, in the meantime, Mr. Latourette had been succeeded as your attorney by Messrs. Teiser and Keller? [43]      A. Yes.

Q. And Mr. Erickson offices with Messrs. Teiser and Keller, does he?

A. They are in the same suite there in the Morgan Building.

Q. And were at all times since your appointment as Trustee?      A. Yes.

Q. Or at least since his employment?

A. Yes.

Mr. Teiser: If your Honor please, I ask that the witness not answer that question as to whether the auditor, Mr. Erickson, was employed on a con-

(Testimony of George M. McBride.)

tingent fee basis. I object to that question, unless the basis on which he was employed is gone into. I do not know what difference it would make anyhow. As a matter of fact, he was not on a contingent fee basis.

Mr. Reilly: You say he was or was not?

Mr. Teiser: He was not. The question asked and the witness' answer might leave the impression that there was something mysterious and some impropriety in the employment of an auditor or the fact that he has his office in the same suite I have.

The Court: I am not going to pay any attention to that, gentlemen.

Mr. Reilly: The only purpose of the question, the only reason for the contingent fee part of it and the association of his attorney is to show the availability of assistance, because of the allegations in the complaint to the effect that they were unable, for financial reasons, to make an investigation. [44] That is the sole purpose of it, your Honor, and since we are questioned about that I would like to get——

Mr. Teiser: If you are looking for that exhibit——

Mr. Reilly: I will look at that later, if I may, and produce it, because the exhibits are not in order.

Mr. Teiser: I think it is 107.

Mr. Reilly: 104. No, that is wrong, 112.

Mr. Teiser: That is right. 112 is the exhibit.

Q. I hand you herewith Pre-Trial Exhibit 112,

(Testimony of George M. McBride.)

which is admitted to be a letter received by you from Mr. Erickson, which will give you the date, from which you can see that you were employed in 1936. Is that correct?

Mr. Teiser: I would like to make an objection to this letter when it is offered.

Mr. Reilly: I am asking about the date, first.

Q. Was the arrangement provided for in that letter confirmed and adopted?

A. Well, whether this was the amount allowed by the Referee or whether this was actually used for a basis, I cannot say right now, but this evidently was.

Mr. Teiser: We admit that was the basis. As a matter of fact, it was the basis of the allowance.

Mr. Reilly: We will offer the letter in evidence, your Honor, that being the one which we say is a contingent fee arrangement. [45]

Mr. Teiser: If your Honor please, I object to Mr. Reilly's statement that the reason he is offering this letter in evidence is because it was on a contingent fee basis, that the accountant was employed on a contingent fee basis, and the plaintiff therefore had the services of the accountant available at any time, perhaps presumably without charge, I take it, unless there was recovery.

Mr. Reilly: If he did not recover anything, there is no charge——

The Court: Let us not argue. If you have any objection, make it to the Court and I will rule.



(Testimony of George M. McBride.)

Mr. Teiser: I maintain that this is not an agreement——

The Court: I do not want to hear any argument. Do you want to object to its admission?

Mr. Teiser: I object to the admission of this document.

The Court: All right. It is ruled out.

Mr. Teiser: I object to its admission.

The Court: It is ruled out.

Mr. Teiser: Pardon me.

Q. Mr. McBride, when was it that you first learned of the fact that there was some litigation back in 1931, in this court as well as in the Circuit Court of Oregon, for Multnomah County, in which charges were made to the effect that Mr. Farrington had misappropriated monies of the Western Bond and Mortgage Company? [46]

A. I could not say that I was cognizant of what had been done relative to that litigation. I knew there had been some litigation, but I did not know exactly what, and I could not state at what time I even heard about that litigation and what it was at all. I never was familiar with it. I did not know about the details of it at all.

Q. Tell me, as closely as you can, when you first learned that there had been any such litigation?

A. —I cannot tell you that at all.

Q. Give me an approximation. You can tell within fifteen years, certainly.

A. Well, I did know of it here just within the last—since this started.

(Testimony of George M. McBride.)

Q. Is that the first you heard of it during all that time?

A. Well, it possibly is not. I would not say because those cases that had been brought, or might have been brought—even dismissed or whatever happened to them—I really did not know what the details were. I didn't really go into that very thoroughly.

Q. That is not the question I asked you. I am asking you when you first heard that there had been some litigation back in 1931 involving Mr. Farrington.

A. Well, I could not say that I—when I heard that there was any litigation. I think, however, that I probably had heard that there was some litigation back prior to my time, but what [47] the details of it were I didn't know, and it may have been any time within the first three or four years. That would be my idea of it at this time because then would be the most likely time I would hear it.

Q. When you say "the first three or four years," you mean the first three or four years subsequent to your appointment as Trustee or as Receiver?

A. Yes. If I heard about it enough to pay any attention to it—I heard so many things, and those things which were not immediately necessary for the investigation, many of them, were not paid much attention to—the situation that had happened before my time, which did not appear to be necessary for me to take up.

Q. When you heard of that prior litigation,

(Testimony of George M. McBride.)

which you have now narrowed down to somewhere from 1934 to 1938, did you make any attempt to find out anything about it?

A. Well, not specifically. I don't believe those cases came up, and were dead, as far as I know. I did not even know what the title of the case was.

Q. The answer is "no". You did not make any effort whatever, is that right?

A. No, not that I remember of making any effort to find out what they were.

Q. Did you ever talk to Mr. Agnew, the Seattle attorney for the Western Bond, about prior litigation?

A. I never talked to Mr. Agnew for to exceed ten minutes all the [48] time I was there. I never saw him but that one time. He merely came in and passed the time of day. We did not go into any details on any particular thing and——

Q. Did you find any files of the Western Bond and Mortgage Company with reference to such litigation? A. Not that I remember of.

Q. Didn't Agnew get paid any fees?

A. What is that?

Q. Didn't Agnew get paid any fees by Western Bond?

A. He might have. I would not know. He probably obtained fees for his work as attorney; undoubtedly would pay the attorney, but I would not know—I would not question attorney's fees which were paid, and they had more or less litigation all the time on one thing and another—fore-

(Testimony of George M. McBride.)

closure of mortgages and suits and various things, and I would not know Mr. Agnew's fee particularly. I probably saw it at the time that I looked over Western Bond and Mortgage Company books—undoubtedly would see it, but I don't remember now, ten years from then, what attorneys' fees were paid to the different ones. I could not tell at all.

Q. Did you find any correspondence in the Western Bond files, between the Western Bond and Mortgage Company and Mr. Agnew of Seattle about the litigation that was pending back in 1931?

A. Not that I remember of.

Q. Did you go back and examine the petition for adjudication in [49] bankruptcy, which was filed, as I recall, in November, 1931?

A. Well, I suppose I had seen the petition. I undoubtedly did. The attorneys were supposed to look after that part of it, but I undoubtedly saw it.

Q. Did you discuss with the attorneys who filed the petition the affairs of the Western Bond in 1931 and the litigation which was then pending?

Mr. Teiser: What petition are you speaking of?

Mr. Reilly: The petition for adjudication in bankruptcy.

Mr. Teiser: If your Honor please, I suppose the question might have a bearing in showing there was a petition in bankruptcy, but it has no bearing whatsoever as the fraudulent nature of the transactions which may be uncovered, and a petition in bankruptcy in this or any other case would simply

(Testimony of George M. McBride.)

set forth the fact of bankruptcy, and I take it that this is an immaterial and irrelevant question.

The Court: I want again to suggest that I do not want any conversation between attorneys. We are not trying this case that way. If there is any objection, make your objection to the Court and I will rule.

Mr. Teiser: I thought that is what I did. I intended to make an objection.

The Court: I do not want any conversations going on between the attorneys.

Mr. Teiser: I apologize, your Honor, for that. [50]

The Court: I do not want any apology. I do not want any more conversations between attorneys about any of these things. If there is any objection, make it and I will rule on it. I will overrule this one. Go ahead.

Mr. Reilly: I think there is an unanswered question.

The Court: Yes. Read the question.

(Pending question read.)

A. No.

Q. Did you ever hear of the case of Brockie against the Western Bond and Mortgage Company and other defendants, including the defendant Farrington, up until after the present lawsuit was brought by you in this court?

A. Well, I probably did, but I did not tax my mind with it. As I say, it was not anything that was, I think, in litigation at the time after I took

(Testimony of George M. McBride.)

over, and I did not tax my mind with. I doubt if I knew the title of the case at the time. I could not remember the names of any of those cases until I saw the name of it here. Mr. Teiser mentioned them just yesterday, I think.

Q. Did you make any attempt to communicate with any attorney representing any parties in either the Brockie case or any other litigation that was pending in 1931? A. No, I did not.

The Court: Mr. Reilly, it is evident this is going to take some time. [51]

Mr. Reilly: I think I am pretty nearly through, your Honor.

The Court: If this is a convenient place, I would suspend.

Mr. Reilly: Well, it is, your Honor, because there is one branch of it I would like to look up.

The Court: Court will suspend until two o'clock. I may say I do not intend to run much past four o'clock this afternoon.

(Thereupon at 12:30 o'clock p. m. a recess was taken until 2:00 o'clock p. m.) [52]

Court reconvened at 2:00 o'clock p. m. November 28, 1944, pursuant to recess.

GEORGE M. McBRIDE,

the plaintiff herein, having been previously duly sworn, resumed the stand and further testified as follows:



(Testimony of George M. McBride.)

Cross-Examination (Continued)

By Mr. Reilly:

Q. Mr. McBride, from your investigation, you discovered that Mr. Farrington had sold his stock, or the stock that he owned or controlled, in the Western Bond and Mortgage Company to a Seattle interest, in December 1930?

A. Yes, I knew that he had sold his stock to—I believe to Mr. O'Flynn or a company that was controlled by Mr. O'Flynn.

Q. The Massachusetts Mortgage Company?

A. Yes, which Mr. O'Flynn controlled.

Q. You knew that he had retired from the directorate of the company and was no longer an officer or director after December 20, 1930?

A. Well, whatever that date was; about that time. I knew it from the records, from the corporation records, yes.

Q. You got in possession of the books of the Western Bond and Mortgage Company, and its subsidiaries, in the summer or fall of 1934, four years later?

A. Yes. [53]

Q. Now, at that time or since that time, did you make a search for the books of the Keystone Finance Company?

A. Well, not specifically, I think, just at that time, but I aimed, as nearly as I could, to locate all these various things, and the Keystone Finance Company was one of the subsidiaries.

Q. In any event, not later than 1936, or, of

(Testimony of George M. McBride.)

course, before the filing of the petition for leave to sue the Bank of California, you did look for the Keystone books, did you?      A. Yes.

Q. And you were not able to find them?

A. Oh, I think we found some of the Keystone books. Right at the moment, I do not remember, but my recollection is that we had some of the Keystone books, anyway.

Q. You found a stock book. I think that was among the exhibits, so you found that.

A. Well, I believe so, as I remember now.

Q. What else, if anything, did you find?

A. What is that?

Q. What else, if anything, did you find of the Keystone Finance Company?

A. Well, I cannot answer you offhand. I would show in the records, however, but I can't right now remember the details as to what we found there.

Q. Let me call your attention to your testimony in the case of McBride against the Bank of California, when you were examined [54] by Mr. Thompson.

I will ask you whether the following questions were not asked you by Mr. Thompson and if you did not make the following answers:

“Q. We are not willing to do that. We have asked to have you produce the books. We want them here, these particular ones I have asked to have brought here.

“Mr. Teiser: Keystone Finance Company books?

(Testimony of George M. McBride.)

“Mr. Thompson: Keystone Finance Company books.

“A. So far as my recollection goes, we have never been able to find those books. I don’t know just what books you refer to, but my best recollection now is that Mr. Erickson and I looked for those books but were unable to find them, whatever they may be.”

I will call your attention to some of your testimony, to refresh your memory.

Do you remember having that question asked you and making that answer?

A. Well, not specifically; specifically, no, I do not just remember what questions were asked me. Of course, at that time it was closer to the time that I had been going into these matters.

Q. Were you asked this question by Mr. Thompson:

“Q. I will have to press you, George, just a little. Did you make any effort to find books of account of the [55] Keystone Finance Company at all in response to this request?”

And the answer:

“A. Well, we made efforts originally to find them. I haven’t made any special attempt since this, for the reason that Mr. Munro went down there with me and we looked for any books which might throw any light on this subject, and I assisted him and felt that anything that we could find or that Mr. Munro could find had been found.”

Do you remember that question and answer?

(Testimony of George M. McBride.)

A. Well, I don't—I can't remember just what I did say or what I testified to at that time, but my recollection is that Mr. Munro who Mr. Thompson was talking about was an accountant we sent down there to try and find some of these books for the purposes of the trial, or for whatever purpose he wanted them for, and that he looked for the books, I suppose, according to this testimony here.

At this time I would not remember it offhand that we did, or whether we didn't, but if I testified to it at that time, when my memory was fresh, I suppose it is correct.

Q. I will ask you whether the following question was asked by Mr. Thompson and whether your answer was as stated:

“Q. Mr. McBride, you spoke about there being tons of those old records. Have you been through all of those, so that you know what is there?

“A. I have been through them, I believe, through [56] everything except the individual files, correspondence files, on canceled bondholders. There is a vast amount of those, thousands and thousands of them, and they would produce no results by going through them, so far as I know, and unless there was some specific reason for it there seemed no reason for going through them. However, I have been through even thousands of letters and those various things, and I went through all those books to determine anything which appeared to be relevant. I can't keep it all in my mind now, of course, after three or four years' time. I spent

(Testimony of George M. McBride.)

a year, I suppose, going through all the various records in order to run down the various angles of the thing."

Do you remember so testifying?

A. I do not remember that specific testimony, but——

Q. Is that testimony a fact?

A. This was with relation to the Bank of California, however.

Q. Was the following question asked of you and did you make the following answer:

"Q. All right, and I beg your pardon for not having clear in my mind exactly what it was. Now, aside from those correspondence files, then, I will say that you have been through these records that you mention sufficiently so that you can tell whether a certain set of stuff—I don't care about the particular books—of Keystone Finance Company books are or are not there?" [57]

To which you answered:

"A. Right now, from my recollection of having gone through them, I would say that very little of the Keystone Finance Company's accounts which would reveal anything really of importance. Whether there is anything there, I wouldn't say."

Do you recall so testifying?

A. I suppose that is correct, if that is what I testified to.

Q. And did you testify in this fashion:

"Q. All right. Now, this item of Books of Account of Keystone Finance Company showing dis-

(Testimony of George M. McBride.)

position of moneys deposited in The Bank of California, N. A., when the mortgages in litigation in this matter were executed?

“A. Well, since testifying this morning, and after refreshing my mind somewhat in going over the records, I would say positively that we never did have those books. We made an effort to find them, and I know that Mr. Erickson and myself searched very diligently to find those books of the Keystone Finance Company and made inquiry from Miss Gallagher about them, I remember that, but we were unable to find them.”

Did you so testify?

A. Yes, I believe so.

Q. Do you remember now? Can you answer my question as to whether the bulk of the books of the Keystone Finance Company are missing? [58]

A. Well, that would appear to indicate that they were, and my memory at that time was better refreshed than it is now, because right now I really would not swear to it at all, other than what is testified to there.

Q. What do you say now? Do you know where the books of the Keystone Finance Company are?

A. No, I don't right now.

Q. The Massachusetts Mortgage Company's manager or agent was a man named O'Flynn, wasn't it?

A. Yes.

Q. You stated maybe the sale of the Farrington stock was to O'Flynn, or the mortgage company. That is the man you are referring to?



(Testimony of George M. McBride.)

A. Yes, O'Flynn; he was the leading light of the Massachusetts Mortgage Company.

Q. You know, from your investigation, that Mr. O'Flynn conducted the negotiations leading up to the sale, on behalf of the Massachusetts Mortgage Company, do you not?

A. I do not know anything about that part of it, who negotiated it, or how it was led up to, or anything about that part of it.

Q. You know that Mr. O'Flynn participated in it?

A. Well, undoubtedly he participated in it, if he bought the stock.

Q. Yes. Is Mr. O'Flynn now living? [59]

A. No.

Q. How long has it been that he died?

A. I can't tell you, but I know he has been dead for some years. I don't know how long.

Q. He was dead prior to the institution of the present action? A. Yes.

Q. Do you know what, if any, part in the transaction which involved the sale of the Farrington stock to the Massachusetts Mortgage Company Arthur C. Spencer had?

A. I did not get the last part of the question.

Q. Do you know what part in that transaction, if any, Arthur C. Spencer had? A. No.

Q. You do not know anything about that?

A. No.

Mr. Reilly: That is all. There is one question

(Testimony of George M. McBride.)

I would like to ask, if I may, with the Court's permission.

Q. Did you find any books of the General Loan Company?      A. I don't remember them at all.

Q. You do not know where any books of the General Loan Company can be found?

A. No, I do not.

Mr. Reilly: That is all.

### Redirect Examination

By Mr. Teiser:

Q. Mr. McBride, you have testified to the fact that the [60] attorney general's office paid you for a period of time when you were receiver, and I think extended over a little time when you were trustee, at the rate of \$150 a month.

Will you state how it was that they happened to pay you that amount of money, and the circumstances surrounding the agreement to pay?

A. Well, I was in a position where I could not afford to give all my time staying down there and interviewing the public as they came in about bonds, these bondholders and these various people, and handling various questions that came up. I just could not give the time to it, and I told Mr. Moody, in conversation, that I just could not do it any longer and he suggested that if I would go on through with it, in order for the Attorney General's office to get information about things that came up and the conditions I found there, that they would put me on the payroll and take care of this

(Testimony of George M. McBride.)

expense. We had no money there to pay any expenses. We had nothing. There was \$15.80 there when I took over, that besides a couple of town lots which were not very valuable, were the only things that were free that I could discover. I told him that I just could not afford to, that I did not have the money to go ahead and do that.

Q. Mr. McBride, Mr. Reilly asked you whether or not the Attorney General's office did not pay you \$150 a month and your office expenses, and I think you answered "Yes, for a [61] period of time." The office expenses that was referred to was whose office expense? Your's or the Western Bond and Mortgage Company's?

A. No, the Western Bond office expense. They had quite a large office and also another room which was rented, in part, to other parties, but they were all filled with files and books, and it was necessary to keep them that way so that we could get at the various things relating to the corporation.

Q. All I want to know is: Did they pay your office expenses or not?

A. Personal expenses, you mean?

Q. Your own office expense rather than the Western Bond and Mortgage Company office.

A. Well, I would not say so, no; they did not pay my expenses of my office that I had up in the Failing Building, no.

Q. When did you close that office in the Failing Building?

(Testimony of George M. McBride.)

A. I cannot tell you exactly. I imagine about—I would think probably along about October, but I won't say for certain.

Q. October of what year? A. 1934.

Mr. Teiser: That is all.

Mr. Reilly: That is all.

(Witness excused.)

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## R. ERICKSON

was thereupon produced as a witness on behalf of the plaintiff, and, being first duly sworn, was examined and testified as follows:

### Direct Examination

By Mr. Teiser:

Q. Mr. Erickson, what is your occupation?

A. Accountant.

Q. Are you a Certified Public Accountant?

A. Yes, sir; hold a certificate from the Oregon State Board of Accountancy.

Q. At one time, you were a member of that board, weren't you? A. Yes, sir.

Q. How long have you been practicing accountancy in this area?

A. Public Accounting since 1924.

Q. Where is your office?

A. 738 Morgan Building.

Q. Is that the suite of offices that I occupy also?

A. Yes, sir.

(Testimony of R. Erickson.)

Q. Have you any connection with me in your work other than occupying the same suite of offices I do, the same group of offices?

A. No, sir.

Q. Any compensation that you get or I get in any way passing between us? A. No, sir. [63]

Q. Have you examined the books and accounts of the Western Bond and Mortgage Company?

A. Yes, on several occasions.

Q. Will you state from such examination whether the books, as kept, disclose on their face any improprieties in respect to the matters alleged in the complaint in this action?

Mr. Reilly: That is objected to as calling for a conclusion of the witness, not testimony as to any fact.

The Court: Yes, I think so.

Q. State whether or not the books of the Western Bond and Mortgage Company show on their face any improprieties in regard to the transactions concerning the Western Guaranty matters?

Mr. Reilly: The same objection, if the Court please.

The Court: I think he may answer.

A. No, they do not.

Q. Do they show any improprieties in regard to the transactions concerning Western Bond and Mortgage Company's transfer of 40,000 shares of Consolidated Credit Company's Class "A," no par stock, in return for stock of the Keystone Finance Company?

(Testimony of R. Erickson.)

Mr. Reilly: That is objected to as calling for a conclusion of the witness, not calling for any testimony as to any fact.

(Pending question read.)

The Court: That all depends on what is an impropriety. [64] The Court sustains the objection.

Mr. Teiser: Let me put it this way:

Q. Did the records on the books of the Western Bond and Mortgage Company in connection with the matter which I have just detailed, that is, the transfer of the Consolidated stock for Keystone stock give rise to, or was it of such a nature as would give rise to any question as it was set forth on its books?

Mr. Reilly: That is objected to as incompetent, irrelevant and immaterial, calling for a conclusion of the witness, and not the best testimony as to any fact, depending entirely upon the nature of the witness and not the nature of the books. The books are themselves the best evidence. It seems to me that this is wholly outside of the realm of competent testimony.

Mr. Teiser: If your Honor please, it seems to me that it is claimed here that the books and records of the Western Bond and Mortgage Company were of such a nature that even the Trustee, who was not a Certified Public Accountant, would be caused to be suspicious concerning them and would necessarily cause them to make inquiry concerning those records.

The Court: He may testify as to whether he was suspicious or not, that is true, but for you to say



(Testimony of R. Erickson.)

there was nothing on their face indicating any impropriety or anything that would cause anybody to question them is improper. I have to [65] draw the conclusions. It is not for the witness to draw them for me. The objection is sustained.

Q. Mr. Erickson, as an expert accountant, would you or would you not say, or what would you say—I will put it that way—as to the nature of the entries on the books and records of the Western Bond and Mortgage Company in connection with the transaction which I have just referred to, as to whether or not they cause any question to arise in your mind as to their propriety?

Mr. Reilly: Object to it, if your Honor please, as involving several questions.

The Court: Objection sustained.

Q. What was your reaction as a public accountant to the records of the transaction, as shown by the books, in connection with the transaction as to the 40,000 shares of stock of the Consolidated Credit Company for stock in the Keystone Finance Company?

Mr. Reilly: That is objected to as calling for a state of mind of the witness and not for testimony as to the fact.

The Court: No. If the witness testifies that at that time the layout was such that he was suspicious, obviously, that shows the time when this suit should have been brought. Therefore, I would permit him to answer.

Mr. Reilly: Exception.

(Testimony of R. Erickson.)

The Court: You do not need to take exceptions.

Mr. Reilly: I have got so I don't remember how——

The Court: I thought that probably you were trying to shake the confidence of the court.

Mr. Reilly: I have given up that hope a long time ago.

A. There is a single entry on the books of the Western Bond and Mortgage Company recording this transaction, which recites that the Western Bond and Mortgage Company parted with 40,000 shares of Class "A" common stock of the Consolidated Credit Corporation, for which they received 1500 shares no par value stock of the Keystone Finance Company, and the figures are of equal value for what was parted with and what was received. On the face of it, there is nothing to indicate that there is anything to be questioned in the transaction.

Q. On the face of the books, did you have any question when you examined them?

A. Not at the time when I saw the entry originally.

Q. When did you first discover any reason for suspicion in regard to those two transactions which I have questioned you concerning?

Mr. Reilly: I object to the double nature of the question. I think it ought to be confined to one thing at a time.

Q. Answer one. Answer as to the Western

(Testimony of R. Erickson.)

Guaranty Company stock, and then answer the next question.

A. I would say it was in June or July of 1943.

Q. When did you discover any questionable thing, anything of [67] a questionable nature, if you did discover it, as to the transaction concerning Keystone and Consolidated Credit?

A. It was at the same time. It was all in connection with the same examination and report that I was making.

Q. You had examined these books before, had you not?      A. Yes, on several occasions.

Q. You had examined them, I believe, in connection with the discovery or ascertaining of some data concerning the transaction in regard to The Bank of California transaction, which was the occasion of a suit in this court?      A. Yes, sir.

Q. At that time did you discover anything in connection with these two matters?

A. At that time, I saw these two transactions were recorded, and looked into them, particularly, however, with regard to whether they had any effect on The Bank of California matter and, finding that they did not, put them aside and did not refer to them until on a later occasion.

Q. When did this later occasion occur, and when did you discover the questionable character of the transactions which they related to?

A. I have stated that was in June or July, 1943.

Q. Will you state how and the circumstances concerning your discovery of the situation, who em-

(Testimony of R. Erickson.)

ployed you, and what was the data you had and how you discovered it generally, without going [68] into any minute details at all; just so the court can understand and can know how it came about, how you discovered it then and had not discovered it earlier.

A. At about the time the United States Government was pressing its claim, as I recall, against the bankrupt estate, their claim for income tax for the year 1930, and Mr. McBride employed me, through yourself, to make an examination of the claim of the Government and to see whether it was in order, or if there were features about it that would offset it or reduce it, or eliminate it, to find out what they were and make a report.

Q. That was in regard to taxes?

A. I beg your pardon?

Q. That was in regard to taxes?

A. That was in regard to income tax for the year 1930. In connection with that claim and that engagement, I asked you to secure for me the original agent's report. There had been an amended report made that same year, and a copy of the amended report was in the Western Bond and Mortgage Company files. The original report, however, was not there, and I had never been able to find it, although I had looked for it previously and had asked if it were available.

I received the report and examined the point on which the Government was asserting their claim, and, in going through it, noted that the transac-

(Testimony of R. Erickson.)

tion of the sale of the [69] Western Guaranty Company stock was tied in with the sale by Mr. Farrington and the Laurel Investment Company of their holdings in Western Bond and Mortgage Company to O'Flynn, or to the Massachusetts Mortgage Company, and, if I recall, I brought the matter to your attention, and you asked me to make quite a thorough report on the situation.

After I had reviewed the Government's points on which they were asserting their claim for taxes, I made a further examination of the books to determine whether there were any losses not shown by the books that offset the Government's claim, and, in checking back, I noticed the record of the dissolution of the Keystone Finance Company in 1930 and the fact that item had been added to the value of the stock, when there was no transaction occurring to give rise to it. In 1943——

Mr. Reilly: Will you state when in 1930—pardon me—was this transaction?

The Witness: That was in December.

Mr. Reilly: Was that the transaction that Farrington was in?

The Witness: I think it was December 15, 1930, that that Keystone liquidation was recorded. I would not be positive, but I think that was the date.

In the spring of 1943, a client of my office had purchased what is known as the Keystone Ranch from the [70] Bankruptcy Court and he had received an abstract of title to the property, which I had in my office.



(Testimony of R. Erickson.)

The Keystone Finance Company minute book states that stock of that company was paid for by the transfer of some 8920 acres of land, comprising what is known as the Keystone Ranch, for the stock of the Keystone Finance Company in settlement of the original subscription.

I checked back with that abstract that I had and found that the ownership of the Keystone Ranch property, since 1925, had been in the Russell Land and Livestock Company, which corporation was a wholly owned subsidiary of the Western Bond and Mortgage Company.

Q. That was the first time you discovered that situation, I take it?      A. That is right.

Q. And you reported that to Mr. McBride?

A. To Mr. McBride.

Q. Was the matter discoverable from the books alone?      A. I would say no.

Q. The books of the Western Bond and Mortgage Company?      A. That is right.

Q. In regard to the other transaction on which suit was brought, that is, the transaction concerning the stock, the Western Guaranty Company stock, will you state when you first happened to discover that? [71]

A. As I have stated, that was in connection with the examination of this revenue agent's report, in which it is stated that——

Mr. Reilly: Never mind. I object to what was stated in the revenue agent's report.

The Court: Yes.



(Testimony of R. Erickson.)

Q. You mentioned the amended report, revenue agent's report, that you had seen a copy of.

A. Yes, there was a copy or the original, I don't know which.

Mr. Reilly: Is this the amended? Is there more than one of those?

Mr. Teiser: No, there is the original one in evidence, 59. This is 60.

The Court: Here is the other one.

Mr. Teiser: That is not what I want, your Honor.

Q. Is the paper I now hand you, which is marked Pre-Trial Exhibit 60, the amended return or report of the revenue agent which you saw, or a copy of which you saw, and which you referred to previously as having seen?

A. I believe this is, yes. I don't know whether this was the one I saw or whether I saw the copy of it, but that is undoubtedly the one that I saw.

Mr. Teiser: I ask that it be marked with the same number and introduced in evidence.

Mr. Reilly: We make the same objection to this as to the [72] prior one, your Honor, and if it is limited only to the purpose of serving as an excuse for the delayed bringing of the suit, we offer no objection to its use for that purpose.

Mr. Teiser: That is the sole purpose.

Mr. Reilly: We object to it being considered as to the truth of any statements. I do not know what is in it.

The Court: Admitted.

(Testimony of R. Erickson.)

(Copy of letter dated May 7, 1943, from Treasury Department, Washington, D. C., to Collector of Internal Revenue, Portland, Oregon, heretofore marked Plaintiff's Pre-Trial Exhibit 60, was thereupon received into evidence and marked Plaintiff's Exhibit 60.)

Q. Does that amended return give any information at all of the nature that you referred to?

Mr. Reilly: That is objected to. The document speaks for itself in that particular.

The Court: He may tell what his reaction was. The objection is sustained. Put another question.

A. That is not——

Mr. Teiser: Wait a minute.

The Witness: Pardon me.

Q. State what your reaction was to the amended return that you have in your hand, or a copy of it, when you first saw it.

A. That is not the return, Mr. Teiser. [73]

Q. I do not mean the return; the report.

A. It is amended and it is referred to here as a revised report and it does not touch on any of the two matters that I have heretofore mentioned.

Q. Just making some adjustment of the taxes?

A. It gave the company some relief on the originally asserted tax.

Q. Do you know whether or not, after you gave the information to Mr. McBride in connection with these two matters, any further steps were taken by him or by you, at his request, in regard to discov-

(Testimony of R. Erickson.)

ering further facts or verifying the facts that you reported?

A. Yes, there were further steps taken.

Q. What, for instance, without telling the result of those steps?

A. Well, you and myself made a trip to Seattle and to Everett, Washington, to inspect the books of the Western Guaranty Company. We had ascertained that the records of the Western Guaranty Company were had by a party that at one time had been connected with Western Bond.

Q. Do you know whether or not the Referee went up to Seattle with us on that occasion?

A. Not on that occasion. The gentleman's name is Bennett Baldy. [74]

Q. The Referee went up to Seattle with us?

A. No, sir.

Q. Do you know whether the Referee made arrangements to have available the books for examination by you?

A. Which books?

Q. The books of the Western Guaranty Company?

A. Yes, sir.

Q. And you made such examination?

A. Yes, sir.

Q. In regard to further steps, I asked you about the Referee going up to Seattle to make a further investigation in regard to Mr. Baldy and the books of the Western Guaranty Company?

A. I don't recall.

Q. Do you recall the Referee going up with

(Testimony of R. Erickson.)

you and me on some trips, or being there together in Seattle?      A. No, I don't, Mr. Teiser.

Q. Do you know whether or not any examinations were held in regard to verifying the matters which were indicated existed?

A. Yes. Mr. Vester was called up before the Bankruptcy Court under what I think is 21-A examination, and Mr. Farrington was called in on examination.

Q. From your knowledge of the books of the Western Bond and Mortgage Company, particularly in regard to the two matters which have been referred to, concerning which you have been questioned, let me ask you whether or not anyone in authority, [75] having knowledge of the facts, the true facts, in connection with those matters, could have made the entries on the books, or could have caused the entries to be made on the books that were made thereon, without a purpose to deceive and——

Mr. Reilly: That is obviously calling for a conclusion of the witness.

The Court: The objection is sustained.

Mr. Teiser: I do not want to argue with your Honor, but may I state my reasons for asking the question?

The Court: No. I won't hear them.

Mr. Teiser: That is all, Mr. Erickson.

(Testimony of R. Erickson.)

Cross-Examination

By Mr. Reilly:

Q. Mr. Erickson, you were first employed in this matter in 1936?           A. Yes, sir.

Q. And when, in 1936?

A. June or July. I would not be quite sure as to which month, but I think it was the last of June.

Q. On what terms?

A. The terms of my employment were contained in a letter that I addressed to Mr. Teiser or to the Trustee.

Q. Regardless of whether they are contained in a letter, what were the terms on which you were employed?

Mr. Teiser: I object to that, if your Honor please. I take [76] it that the matter referred to is not this particular matter but the matter of The Bank of California.

Mr. Reilly; No, sir.

The Court: Just a moment. I am fully capable of ruling, without letting you do it. I think he may answer as to what the terms of his employment were. He should know.

Mr. Teiser: May I ask your Honor to have the question made a little more specific as to what matter he is talking about?

The Court: Don't answer for the witness. If the witness does not understand the question, he may say so. If you do not understand the question, it don't make any difference.

(Testimony of R. Erickson.)

Mr. Teiser: It is a little hard for me to make an objection unless I know what he is talking about.

The Court: I think you can make objections. Let the witness answer, if he can.

(Pending question read.)

A. I have forgotten now, Mr. Reilly, the exact terms.

Q. Let me ask——

A. May I continue?

Q. Let me ask you whether your employment was—if compensation was fixed for all services you might render in connection with the Western Bond?

A. No, I would not say that, Mr. Reilly. If I might have my letter, I will give you the basis of it.

Mr. Reilly: Will the bailiff please hand the witness pre-trial exhibit 112?

The Witness: The terms under which I was employed were that if funds came into the estate——

Q. From any particular source or from any source?      A. From any source.

Q. Go ahead.

A. If funds came into the estate to the extent of \$10,000 and no more, I would be agreeable to having the Referee fix my fees at whatever he might determine they were worth.

That if an additional \$15,000 came in, that the rate would be for twenty-five days' time, if it ran that much, at \$50 a day and the next twenty-five days at \$25 a day; anything above that, to be \$20 a day.

If an additional \$25,000 were to come into the es-



(Testimony of R. Erickson.)

tate, it would be twenty-five days at \$50 a day; the next twenty-five at \$40 and any additional time at \$25 a day.

And that in the event the funds coming in were to the amount of \$25,000 additional, it was to be fifty days at \$50 a day and the next fifty days at \$35 a day; and that if the total funds coming in exceeded \$100,000, the compensation was to be at \$50 for all time devoted.

I would like to explain the reason for this arrangement.

Q. I am not interested in the reason for the arrangement. I just want to know what the arrangement was. I am not criticizing [78] the arrangement, Mr. Erickson.

A. I should like to explain.

The Court: Wait. Wait just a minute, if you will. Just answer Mr. Reilly's questions.

The Witness: All right, sir.

Q. These moneys which you have detailed, so much per day, those were to be paid for your services?

A. That is right.

Q. And you were to be paid for those services, contingent on the amount of money that came into the estate?

A. That is right.

Q. Regardless of the source from which it came?

A. That is right.

Q. There was no limitation that it had to be the result of your services?

A. No.

Q. You were to get the money, dependent upon the amount of money that came into the estate?

(Testimony of R. Erickson.)

A. That was my understanding when I wrote the letter, yes. As I recall, that was Teiser's understanding. We had talked it over at the time.

Q. How long have you lived in Portland? Were you living here in 1931?

A. I lived in Portland for about six months at one time. I do not live in Portland. [79]

Q. You do not live in Portland? A. No.

Q. I mean Portland or the immediate vicinity?

A. Some fifty years.

Q. Some, what? A. Fifty years.

Q. Fifty years? A. Yes.

Q. And you were taking the Portland papers and have during most of that time?

A. Yes, sir, some twenty-five or thirty or more years; I have read the Portland papers off and on.

Q. You were taking the Oregonian or Journal, or both in 1931? A. Oh, probably.

Q. Did you know nothing of the affairs of the Western Bond prior to that employment in 1936?

A. I did not hear all that question.

Q. Did you, as a citizen of Portland, reading the papers, know nothing of the affairs of the Western Bond and Mortgage Company or the litigation about it prior to 1936?

Mr. Teiser: I object, if your Honor please, to this line of questioning. Whether the witnesses knew or did not know, if he did not impart it to the Trustee, I do not see that it makes any difference. What we are trying to find out now is how the Trustee came to this knowledge and what sources

(Testimony of R. Erickson.)

available to the Trustee there were for knowledge.

The Court: It is of very little weight, I assure you. I think I might as well make my attitude plain. I do not think, as a matter of fact, that something that appeared in the papers has much to do with it, that is, what a person who casually reads the papers has to do with it, or what they think about it or whether it was ever called to their attention. Unless you have some specific reason for looking at a paper, I would say right offhand it would have nothing to do with it.

Mr. Reilly: I was hopeful that the witness would answer that he did know about this.

The Court: He may answer.

A. I had seen references from time to time in the papers of the difficulties of the Western Bond and Mortgage Company, but when they were and when I saw them, I haven't any recollection.

Q. And about litigation about it?

A. Yes, I think I had seen something about some litigation, where they had also sued some other concern.

Q. The Universal?

A. The Universal Bond and Mortgage Company, I think I remember seeing that reference to that suit also.

Q. In respect to this Western Guaranty transaction, that whole transaction was set up on the books and in the Journal and in the minute book, was it not?

A. There is a journal entry recording the dis-

(Testimony of R. Erickson.)

position by the [81] Western Bond and Mortgage Company of the stock in the Western Guaranty Company, for which they were supposed to have received certain assets, and there is a recital of the transaction in the minute book.

Q. And the sole question involved in the Western Guaranty transaction is one of value, is it not, whether the Western Bond in the trade of the assets it got for the stock of the Western Guaranty Company got fair value? That is the whole question, isn't it?

Mr. Teiser: I object to that question as a question of law, if your Honor please.

The Court: The objection is overruled. It is part of the cross-examination.

A. Well, I would not say that that was the sole question involved in there, Mr. Reilly.

Q. What other question was involved?

A. Simultaneous transactions where assets were supposed to have been used in two transactions, one for the sale of the Western Bond and Mortgage Company stock to O'Flynn, and then the simultaneous sale by the Western of its stock in the Western Guaranty Company.

Q. The transactions are set up, are they not, in the books?

A. There is no reference in the books to the sale of the stock to the Western Bond and Mortgage Company by Mr. Farrington and the Laurel Investment Company to O'Flynn or the Massachusetts [82] Mortgage Company.

(Testimony of R. Erickson.)

Q. The minute book shows Mr. Farrington and Mr. McCroskey went out of the company, out of the management, the directorate of the company, and Mr. O'Flynn and his associates came in, do they not?      A. Yes, they do.

Q. And at the meeting held the new officers, the transaction, the trade of the Western Guaranty for certain assets occurred——

A. I do not understand that.

Q. I say, the books do show that at the meeting following Mr. Farrington and Mr. McCroskey going out, the Western Guaranty transaction, the trade of stock of that company for certain assets took place, didn't it?

A. The minute book shows that there was a meeting, I think on December 20, 1930, when Mr. Farrington and Mr. McCroskey, I believe, resigned, and Mr. O'Flynn and someone else took his place.

The minute book recites that there was an adjournment of thirty minutes and in the minutes following this recital of the adjourned meeting is set forth the trade of the Western Guaranty stock for those other items that were supposed to have been received.

Q. That transaction is fully recorded, isn't it?

A. Those items are set forth in the minute book, yes, sir.

Q. And they are referred to again at a later place in the [83] minute book, are they not, some two weeks or so later?

(Testimony of R. Erickson.)

A. Yes, I believe they are. There was a stockholders' meeting later at which this was ratified.

Q. So that the transaction was there for anybody to examine that wanted to?

A. What is recited there is easily read, yes.

Q. Did you ever know about the lawsuit over that transaction that was filed in this court? Did you ever discover anything about that?

A. I never heard of it.

Q. You never heard of it? A. No.

Q. You did not make any appraisal of the assets that the Western Bond received in that transaction, did you? A. No, I did not.

Q. If the Western Bond in fact received assets of greater value than it parted with, why, then, there isn't any case, as far as you know?

A. There isn't any what?

Mr. Teiser: I object to the question, your Honor. The question, obviously, is argumentative. If answered one way, it would excuse his not discovering or, having discovered the situation here, if full value was received for the assets, then he could not have discovered it or, if he discovered anything, it would have been all right. If, on the other [84] hand, he had discovered what he did discover, then he would have reason to bring it to the attention of the Trustee.

The Court: I will listen to the witness.

(Question read.)

A. Well, I think that would be true. If they did actually receive assets of value compared to what



(Testimony of R. Erickson.)

they parted with, they could not question the transaction.

Q. All right, then. I will try to come back to the same question, that the matter in issue here is the value of the assets and not the state of the books.

A. Is that a question?

Q. Yes. Is that a fact?

A. Will you repeat that question?

The Court: Read the question.

(Pending question read.)

Q. Is that right?

Mr. Teiser: I object to that question, if your Honor please, as argumentative and not proper cross examination.

The Court: Overruled. Here is an expert on the stand who has gone over these books. I think I will let him answer.

Mr. Teiser: I tried to qualify him as an expert to answer expert questions, and your Honor would not permit me to do it.

The Court: Yes, I know, but you were asking something different.

A. Well, I think there is considerable question on the [85] transaction, Mr. Reilly. It is true——

Q. All right. You think there is something else involved? A. Yes.

Q. What was it you discovered in these books, in addition to what is them now, in respect to this Western Guaranty transaction?

Mr. Teiser: If your Honor please, I hope you won't object to my objecting so frequently, but it

(Testimony of R. Erickson.)

seems to me that is a question which we are not discussing here, as to what is wrong with the transaction; that the question we have got to determine in connection with what we are here engaged in is whether or not there was any laches on the part of the Trustee. It does not seem to me that the factual situation is what we are trying here at this time, and that is what this question has to do with.

The Court: If I did not think it had some pertinency to what we are trying, I would not admit it. In other words, your objection is that it is immaterial, but I do not think so. I think it is material and proper. He may answer.

A. The material fact is the simultaneous character of these transactions, the use of the assets for two purposes simultaneously and the further fact that the assets were shown to have had no value.

Q. Eliminating the question of value, now, because all of that goes to the merits—— [86]

A. May I correct that? There were some assets there of a minor amount that apparently had value.

Q. Well, I won't go into that part of it. Where did you discover that the transactions were simultaneous?

A. In the revenue agent's report is where it is set forth.

Q. Is it not in the minutes?

A. No, sir. The minutes don't show anything with regard to what the form of payment was to Mr. Farrington and the Laurel Investment Company for the sale of the stock.

(Testimony of R. Erickson.)

Q. It shows that it was Western Guaranty stock that they got?

A. No, sir. There is nothing to show where they got those items or that those were all of the items that were comprised in their exchange, in Farrington and the Laurel Investment Company's exchange with O'Flynn and the Massachusetts Mortgage Company.

Q. Then, as I understand it, the only thing you discovered, outside of the question of value, was that you discovered Mr. Farrington had received these assets, or some of them, for his stock, just a little while before, which he traded for the Western Bond—for the Western Guaranty stock? It was purely a question of time, is that the idea?

A. I couldn't say it was merely a question of time, Mr. Reilly.

Q. And the source of their acquisition of the assets?

A. Partially, yes.

Q. Let me get this straight. The only thing that you claim to [87] have discovered, outside of this question of value, that is shown on the face of the books was that the assets which Mr. Farrington and the Laurel Investment Company traded for the Western Guaranty stock had been acquired by Mr. Farrington or Laurel, or both of them, just a little while before the Western Guaranty transaction took place?

A. Well, I would not say that. It was not just a little while before, apparently, from the records,

(Testimony of R. Erickson.)

which I have seen of it, in reference to it. It was simultaneously with it.

Q. That is the only thing that occurred?

A. That is the main point that I noted on the transaction.

The Court: Finish your answer.

A. Here is where the net worth of the Western Bond and Mortgage Company, represented by the controlling stock, is exchanged for assets that are immediately traded to the Western Bond and Mortgage Company for a part of its assets, not all of them, but part of them, namely the Western Guaranty stock.

The transaction seems to be a case of where the former owners are stepping out and taking with them certain assets of the company, and that the incoming owner put in some supposed assets to cover the book value of what was taken out.

Q. Well, what you have discovered, then, was that the transaction, you claim, was simultaneous instead of an interval [88] having elapsed, and that Farrington and the Laurel Investment Company had acquired the assets that they used in that trade from the new owners of the Western Bond?

A. That is what I found in the revenue agent's report, yes.

Q. And that is what you are relying upon as the newly discovered matter which you found out?

A. Yes.

Q. It is your contention, as I understand it,

(Testimony of R. Erickson.)

that should have been set up on the books of the Western Bond?

A. I do not contend it, Mr. Reilly. I do not contend that.

Q. That is what you have been talking about, something that is not at all on the books of the Western Bond, isn't it?

A. No, I didn't say that.

Mr. Teiser: Objected to. He has never said that.

The Court: Objection sustained.

Mr. Reilly: I do not know what their objection is. May I ask another question?

The Court: Yes.

Q. Was the source from which Mr. Farrington or the Laurel Investment Company acquired the assets that they traded to the Western Bond a proper subject for entry on the books of the Western Bond and Mortgage Company?

A. No, sir.

Q. Was the time that elapsed between their acquisition of those assets and their transfer to the Western Bond and [89] Mortgage Company a matter proper to be set up on the books of the Western Bond?      A. No, sir.

Q. This information that you received about the so-called simultaneous nature of the transaction, that information, as far as you know, was acquired by the revenue agent solely from the books of the Western Bond and Mortgage Company?

(Testimony of R. Erickson.)

A. I would not know where he obtained his information. However, it is set forth in his report.

Q. You could just as easily have found that from the books of the Western Bond as any revenue agent?

A. Well I think——

Q. If it was even found from the books?

A. If it were in the books, I presume I would probably have been as well able to find it as the revenue agent, yes.

Q. So, any conclusion which you find in any revenue agent report must be his guesses as to what happened, or some private information he had from some other source, is that right?

A. I just had his statement in there of what had happened. No, we were not able to find that. I was under the impression we had traced it down from another source, but I do not recall now just what was done in that respect.

Q. There was no change in the books from the time the entries were made in 1930 until you examined them in 1943, as far as [90] you know?

A. You say, there was no change?

Q. No change in the Western Bond books.

A. Well, I would not know. I saw the books first in 1936. There were entries on there subsequent to 1930.

Q. I mean, in respect to the Western Guaranty transaction.

A. I assume not.

Q. How fully did you examine the books of the Western Bond?

A. When?



(Testimony of R. Erickson.)

Q. After your employment on what I call a contingency basis? A. In 1936?

Q. From then on?

A. In 1936, Mr. Teiser came into the office and he had this matter of the exchange of the Keystone Ranch property, and wanted some assistance in connection with it, and engaged me to assist him in tracing out the entries on the books, and to see what other items might be on there that were subject to action by the Trustee.

I checked through most of the transactions of any consequence to see whether they were concerned with what we might call The Bank of California matter, and I noted most of the major items on there. After I had looked into them to see where they fitted in, or if they did fit in with The Bank of California matter, I put them aside and did not refer to them, I think, on no occasion until a long time later. [91]

After The Bank of California matter, and while it was still pending, there was an action against Besson and Brown, Dr. Besson and Mr. Brown, for recovery, and this had arisen before The Bank of California matter.

Q. That was a minor matter, which was settled for \$3,000 or some such amount?

A. I have forgotten myself what it was settled for, but I think that was about it. I do not recall that I had occasion to look into any of these other matters from then until 1943. I looked in the books afterwards, but generally in connection with The

(Testimony of R. Erickson.)

Bank of California matter; it was concerned mainly with their transaction.

Q. As I understand you, you were employed to investigate generally?

A. That is right, in the original employment.

Q. And that your way to be a percentage of everything that came into the estate, regardless of whether you produced it or not?

A. No, I would not say that was it.

Q. I thought you just said so.

A. No, I did not say it was a percentage of what came in that I was to be paid.

Q. That is not right. I am wrong. It is not a percentage of what came in. I beg your pardon. An amount of money which was rated according to the amount that came into the estate? [92]

A. I may say this: I was to be paid a certain rate for my time, depending on how much came into the estate, and whether it came in from my efforts or from someone else's efforts, or if it was paid to my estate if I was not there, it would still be coming to me.

Q. Turning to the Keystone matter, what was it you claim you found that was not in the books?

A. The books recite that the Western Bond and Mortgage Company parted with 40,000 shares of Class "A" common stock of the Consolidated Credit Corporation, for which they were supposed to receive 1500 shares of no par stock of the Keystone Finance Company.

(Testimony of R. Erickson.)

The Keystone Finance Company minute books state that they——

Q. Don't tell what is in the Keystone Finance Company minute book.

A. The Keystone Finance Company minute books state that they had issued their 1500 shares for the 8920 acres comprising the Keystone Ranch, and that this property was owned by E. C. Tapfer and his wife and a man named Snodgrass who were turning it over to the Keystone Finance Company in settlement of this stock subscription.

The abstract of title shows that the Keystone Ranch of 8920 acres, prior to 1925, was owned by a man named Russell, who transferred it to the Russell Land and Livestock Company [93] in 1925, and then, in 1929, the Russell Land and Livestock Company transferred the property to the Keystone Finance Company, but Tapfer and Snodgrass are not shown as being at any time the owners of the land, and the Russell Land and Livestock Company was at all times a hundred per cent subsidiary of the Western Bond and Mortgage Company.

Q. Then, what you discovered was that the abstract showed that Tapfer did not own the land?

A. I had the abstract in my office, and it does not show that Tapfer or Snodgrass ever had any interest in the land, but that that land was in the name of the Russell Land and Livestock Company.

Q. So, you reached the conclusion that the

(Testimony of R. Erickson.)

Western Bond and Mortgage Company owned the property all the time?      A. Yes, sir.

Q. Did you run across any books of the General Loan Company?

A. I think not. The General Loan Company later became the Consolidated Credit Company.

Q. I cannot answer that.

A. It did. It had two or three names.

Q. I think you are mistaken, Mr. Erickson, but you may not be. Go ahead.

A. I think I can give you the names of it.

Q. Are you talking about the Consolidated Credit Corporation?

A. The Consolidated Credit Company. [94]

Q. That is not the stock we are talking about in this case. We are talking about the Consolidated Credit Corporation.

A. No, the stock was the Consolidated Credit Corporation, but the General Loan Company later became the Consolidated Credit Company.

Q. When you say "later" how much later?

A. Well, I think in 1928 it was the General Loan Company, and in about 1929 it was called the Consolidated Lenders of Oregon, and then later in the same year, apparently, the Consolidated Credit Company. It had three names, from the information that I have.

Q. You mean the name was changed?

A. The name was changed.

Q. Legally?

A. I believe that was the way it was done.

(Testimony of R. Erickson.)

Q. In your examination of the books in 1929, did you find a contribution made to the capital of the company of \$200,000 by Mr. and Mrs. Farrington out of their own funds?

A. You say in my examination in 1929?

Q. Of the books of 1929.

A. There is a record in, I think in the forepart of 1929 of where some assets were turned in by Mr. Farrington, which went into the surplus of the company.

Mr. Teiser: I object to the character of that question. I do not know what business it has in this case whatsoever. [95]

The Court: I do not exactly see myself.

Mr. Reilly: I won't pursue it. I was afraid it was starting to get too close to the merits of the situation.

Q. When was it the Government made its claim first against the Western Bond and Mortgage Company?

A. Well, by that you mean what time it was filed with the Bankruptcy Court?

Q. No. It may have been in the Bankruptcy Court, but I mean the time that the Government first made its claim for income tax.

A. It was a claim for the year 1930.

Q. Yes, and when was it?

A. I think the revenue agent's report here gives the date on which the claim was first made.

Q. October 1932?

A. I do not know the date, but if that is the

(Testimony of R. Erickson.)

date on the revenue agent's report that would be the date on which they first asserted the claim.

Q. You say that the original claim disappeared from the files of the Western Bond, or at least was not there?

A. I had never been able to find it in the files.

Q. But when you first examined the files, you found what you call an amended assessment?

A. Yes, the revised report.

Q. You found the revised report when you first examined the [96] files?

A. In 1936, I found a copy of that, either the original or a copy of that revised report.

Q. In the Western Bond files?

A. It was in the Western Bond files.

Mr. Teiser: When you say "original," I take it you mean the original of the amended report?

The Witness: The original of the amended report is right.

Q. That amended report stated an assessment against the Western Bond of, how much?

A. I cannot remember the figures, Mr. Reilly. It is here and shows for itself.

Q. I do not want to take up too much time. Would you say \$40,000 and a penalty of \$2,000, and, of course, interest from 1930, would be about it?

A. Well, I don't remember the figures. It seems to me it was a larger amount than that, but I may be mistaken.



(Testimony of R. Erickson.)

Q. Maybe it is more than that. This revised report——

A. This revised report calls for an additional tax of \$40,772.61, and a penalty of \$2,038.63.

Q. It would carry interest at what rate?

A. Six per cent per annum.

Q. Six per cent per annum, so that there was \$50,000 involved, roughly?

A. At which time? [97]

Q. At the time you first saw it. A. 1936?

Q. Yes. Well, it would be more than that, I suppose.

A. About \$50,000, about twenty-five per cent added.

Q. And the report showed on its face that there was an original back of it, that is, the earlier report?

A. That is right. That led me to ask for the original report.

Q. How did you obtain the original report?

A. Mr. Teiser obtained it for me.

Q. From where? You don't know?

A. I think he got it from the Internal Revenue Bureau Collector's office, or an agent of the Collector's office.

Q. From your experience as an accountant, is a taxpayer entitled to see that?

A. Assuredly.

Q. Any time he asks to? A. Yes, sir.

Mr. Reilly: That is all.

(Testimony of R. Erickson.)

Redirect Examination

By Mr. Teiser:

Q. You do not know what, if any, trouble was had in getting that report, do you?

A. No, I do not.

Q. Some ten years later? A. No, sir. [98]

Q. Mr. Erickson, in regard to this employment that you were questioned about and the letter which was submitted about your employment, your employment, as I read this letter, was to be, the highest rate, \$50 a day. That is the highest rate you were to get? A. Yes.

Q. I might ask you whether \$50 a day is a reasonable charge for accounting work?

Mr. Reilly: That is objected to as incompetent, irrelevant and immaterial. I am not accusing this witness of anything.

The Court: Overruled. He may answer.

A. It is a fair rate.

Q. Under this arrangement, were you to receive more than \$50 a day under any circumstances?

A. No.

The Court: No, he was not.

Q. Let me ask you to look at the last paragraph in the letter and to state whether or not the Trustee was in a position at any time to stop the amount of work? A. He was.

Q. That you were doing? A. Yes, he was.

Q. Under that letter agreement, may I ask you what work you were required or asked to do by

(Testimony of R. Erickson.)

the Trustee? Was it or was it not only in connection with the Bank of California and the [99] Besson and Brown matters?

Mr. Reilly: That is objected to as leading and suggestive.

The Court: Overruled.

A. Those were the items of work that there was to do, but I understood and did look into other matters in the estate, and I did call attention to a transaction concerning the ranch property near Corvallis, and you, I think, and Mr. McBride went down to see about it and decided that nothing could be done about it.

Q. Yes, you did call it to our attention.

A. Yes.

Q. But is or isn't it a fact that what you were employed for at that time was to investigate in regard to The Bank of California matter and the Besson and Brown matter only?

Mr. Reilly: Objected to, your Honor, because the letter speaks for itself.

Mr. Teiser: No, the letter does not speak for itself.

The Court: Now, just a minute.

Mr. Teiser: I beg your pardon, sir.

The Court: I was inclined to think the letter would speak for itself, but everybody has gone into it. Mr. Reilly insists on asking about it, and, in the first place, asking about his interpretation of it, without him seeing the letter, and in view of that fact—

(Testimony of R. Erickson.)

Mr. Reilly: He had the letter before him. [100]

The Court: Oh, no, he did not, at first. You held it in your hand.

Mr. Reilly: Yes.

The Court: And he asked if he could not see it before he answered.

Mr. Reilly: The reason I did that was because your Honor would not let me put that in evidence on cross-examination.

The Court: I know, but you could show it to him.

Mr. Reilly: Probably it should have been shown to him.

The Court: Over the objection of Mr. Teiser, I said that he could answer as to the transaction, irrespective of the terms of the letter. Eventually, you passed the letter over to him. That is what happened.

(Pending question read.)

A. I was not employed to investigate Besson and Brown originally. That came in later. The original employment was in connection with The Bank of California matter and, as I said, that was what I devoted my time to mainly, but I did look into other matters, mostly, however, as to their past connection with Bank of California matters.

Q. Mr. Erickson, when you were employed to handle the tax matter and related matters arising from the tax matters, the result of this suit, were you employed under a separate agreement?

(Testimony of R. Erickson.)

A. Yes, sir.

Q. And your work under this agreement had all been ended at [101] that time?

A. It had ended.

Q. Had you been paid for it fully, as far as you know, before or sometime before?

A. I was paid for it in 1943.

Mr. Reilly: What year was that? 1943?

The Court: 1943 is what he said.

The Witness: In the early part of 1943 is my recollection as to the time of payment.

Q. That was after money came in to the Western Bond from The Bank of California matter?

A. The Bank of California and the sale of the ranch property.

Q. Have you been fully paid for your services, in the last few days we will say, in connection with your services in this matter?

A. I rendered a bill for my time in connection with the report on the tax matter and the preparation of these separate reports, but since August 1943 I think I have put in some time for which I have not been paid. I may say this. I recall that I rendered a bill as of December 31, 1943 and have been paid up to that time.

Q. The basis of your understanding with the Trustee, and approved by the Referee, is definitely the same per day?

A. That is right.

Q. For work done? [102]

A. Yes, sir.

Mr. Teiser: That is all.

Mr. Reilly: That will be all.

(Testimony of R. Erickson.)

The Court: Just a minute. I want to know something about this.

The Court: Q. What is there with reference to the transfer of the Russell Ranch or the Keystone matter that you did not know during the investigation of The Bank of California transactions?

A. Just this, your Honor: The recital is that the Western Bond and Mortgage Company received assets of value for what they parted with. They parted with 40,000 shares of Class "A" common stock of the Consolidated Credit Corporation, which was written up on the books as of the value of \$3 per share of \$120,000, and from sales and other transactions as of the time that seems to have been the value of the stock.

They were supposed to have received 1500 shares of stock in the Keystone Finance Company. The Keystone Finance Company, apparently, never owned anything except 8920 acres of land that comprised the Keystone Ranch.

The Western Bond and Mortgage Company always had title to that same ranch through their ownership of the stock of the Russell Land and Livestock Company.

They received nothing for the 40,000 shares that they parted with, nothing that they had not previously owned. [103]

Q. Was that not all brought out in The Bank of California case? A. No, sir.

Q. What part was not brought out?



(Testimony of R. Erickson.)

A. The fact that the Keystone Finance Company's stock had been paid for by property that was already the property of the Western Bond and Mortgage Company. I do not recall that anywhere in the record of The Bank of California was that ever touched on.

Mr. Teiser: I think it is a little unfortunate, your Honor, that we use the word "Keystone" in connection with these transactions. I wanted to call it to the attention of the witness at the time that he was being questioned about the stock in the Keystone transaction.

Of course, the Keystone transaction that was involved in The Bank of California case was an entirely different transaction than that involved in this situation. I think that is how your Honor got confused.

The Court: The Russell ranch is involved, I take it?

Mr. Teiser: The Russell ranch was involved. The mortgage on the Russell ranch that was given to The Bank of California was involved in that case, but in this matter the stock of the Keystone Finance Company was said to have turned over to the Western Bond and Mortgage Company for 40,000 shares of stock in the Consolidated, which it owned.

You take, on one side there is 40,000 shares of [104] Consolidated stock. On the other side, there is 1500 shares of the stock in the Keystone Finance. That transaction was one in payment of

(Testimony of R. Erickson.)

the other; had no bearing at all, as your Honor can see, as to the mortgage given on the Russell ranch which happened to be owned at one time by the Russell Land and Livestock Company. Those two transactions were removed, except, unfortunately, it had the name "Keystone" to it. One of them was the stock in the Keystone Finance Company. The other was the mortgage on the ranch which was called "Keystone ranch" which was owned at one time, I think, by the Keystone Company. I am not sure about that.

The Court: But, to a large extent, you examined the ownership of the stock of the Keystone in The Bank of California transaction?

Mr. Teiser: The ownership of the stock of Keystone.

The Court: Yes.

Mr. Teiser: The Ochoco stock was owned by Keystone—not by Keystone, by the Western Bond and Mortgage Company.

The Witness: May I interrupt? The Ochoco stock was never owned by the Western Bond. It was owned by the Massachusetts Mortgage Company.

Mr. Teiser: That is right. I think, your Honor, when you look into the matter—no use of my going into it—that you will find that these two transactions had no connection, one with the other, at all. At any rate, that is the [105] conclusion that we reached.

The Court: The point I am asking the witness

(Testimony of R. Erickson.)

is what portion of this did he not examine in The Bank of California case. I know that this court examined the ownership of the stock in Keystone.

The Witness: That is right, your Honor. It was held by the Western Bond and Mortgage Company, as a result of following this transaction, which occurred in 1929, but the stock in Keystone was paid for by property of the Western Bond and Mortgage Company, held through another subsidiary, the Russell Land and Livestock Company.

The Court: I do not quite see what the purpose of that was, and it is not clear to me what part of this transaction that you are now examining was not clear to you through your investigation of The Bank of California transaction.

The Witness: The point that I did not discover until 1943, your Honor, was the fact that the Russell Land and Livestock Company, the Keystone ranch itself, had been used to pay for the stock in the Keystone Finance Company.

At the time we examined into The Bank of California matter, we did not have the abstract and accepted the record as it was entered on the books. Yet, Tapfer and Snodgrass—Tapfer and his wife and Snodgrass had transferred the Keystone ranch itself, the real property, to the Keystone Finance Company in settlement of its stock. [106]

The Court: Well, I understand this portion about the parties that you have just named, Tapfer and Snodgrass, was not developed in this record, as far as you know?

(Testimony of R. Erickson.)

The Witness: They may have been mentioned in there, in that they were incorporators of the Keystone Finance Company. I think probably that was in the record, but the fact that they did not own the property that it is recited that they paid for the stock is not in the record, as far as I ever recall.

The Court: The Court, in the former case, found at all times the Western had fully owned subsidiaries—the Russell Land and Livestock Company, the Keystone and the Ochoco Farms—and the Referee found on the first hearing that the Keystone was operated and manipulated at all times by the Western Bond and Mortgage Company as its adjunct, subsidiary and agent and for the sole purpose of carrying out its designs and biddings, and was a mere corporate shell, and so forth.

The same state of facts existed as to Ochoco Farms. The development of the Government was commenced in 1929. Title to the Russell ranch was then held by Western in the name of the Russell Land and Livestock Company, a wholly owned subsidiary.

In that year, Keystone was organized and, on December 20, 1929, the Russell Company deeded the Russell [107] ranch to Keystone, apparently no consideration for the transfer, as the value of the stock of the Russell Company from then on is carried as nominal. Then, there are some further developments in that regard that do not relate definitely or

(Testimony of R. Erickson.)

particularly to the mortgages which were under the Court's consideration.

The Witness: The finding that Oehoco was owned by the Western Bond would be incorrect, because they never did own the stock. It was owned by the Massachusetts Mortgage Company. I did not recall a number of these items that you have recited; I don't recall that those were in the record at all, your Honor.

Mr. Teiser: Q. Did you or did you not discover the situation in regard to the 40,000 shares of stock, the Consolidated Company stock, at any time prior to 1943?

A. Oh, yes. I saw the record of the transaction, I think, probably in 1936.

Q. Did it occur to you, from what you discovered at the time, that there was anything improper about that transaction?

A. Not at the time. I don't recall that I had any question of that.

Q. When did you first discover—I think you have stated that.

A. In 1943, when I had the abstract, and I went back to see where they could have had title, that is, Snodgrass and Tapfer, where they had title to the ranch to make the transfer. [108]

Q. Is that the first time you gave any information to the Trustee as to that situation?

A. Yes, sir.

Q. Did that appear in one of the matters connected with the tax situation?

(Testimony of R. Erickson.)

A. No, it did not, but it was one of the matters that I examined into as to a possibility of off-setting——

Q. It was one of the things you discovered in connection with your work in the tax matter?

A. That is right.

Mr. Teiser: That is all.

Mr. Reilly: Q. This minute book of the Keystone Finance Company has been in the files of the Western Bond and Mortgage Company, since you have known anything about those files?

A. I think it was in there in 1936, yes. I am sure it was.

Q. Any investigation of the minutes of the subsidiary corporation would disclose the basis for the stock subscription concerning which you speak?

A. Yes, sir.

Mr. Reilly: That is all.

Mr. Teiser: That is all. That is the plaintiff's case.

The Court: Court will be in adjournment until 10:00 o'clock tomorrow morning.

(Thereupon at 4:00 o'clock p. m., Tuesday, November 28, 1944, an adjournment was taken until 10:00 o'clock a. m. the following day.) [109]



Wednesday, November 29, 1944

Court reconvened at 10:30 o'clock a. m., pursuant to adjournment.

RALPH E. MOODY

was thereupon called as a witness on behalf of the defendant and, being first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Reilly:

Q. Mr. Moody, you are an attorney at law?

A. I am.

Q. A resident, at the present time, of Salem, Oregon?

A. Yes.

Q. You have practiced law in the State of Oregon for a good many years?

A. Yes. I think I was admitted in '87.

Q. 1887?

A. Yes.

Q. You are a member of the bar of this court?

A. Yes.

Q. And of the Supreme Court of the United States?

A. Yes.

Q. Mr. Moody, were you at one time associated with the Attorney General's office of the State of Oregon in some capacity? [110]

A. I was Assistant Attorney General, I think, from about 1933 on to—I think it was March 1938 when I resigned.

Q. In your work as Assistant Attorney General, did you come in contact with the Western Bond and Mortgage Company situation, along in 1934?

(Testimony of Ralph E. Moody.)

A. Yes.

Q. Will you tell how that came about, Mr. Moody?

A. Mr. Charles Goodwin, who was attached to the Corporation Department of the State, came over to the Attorney General's office. I do not remember whether he came directly to me first or whether he went to the Attorney General, Mr. Van-Winkle, and the matter was referred to me.

In any event, I handled the matter, and he stated the Western Bond and Mortgage Company was in a situation that was giving the department a good deal of trouble, and that they had filed an application in Bankruptcy.

I gave the matter considerable thought and study to see what we could do. I found a particular statute in the state that authorized the Corporation Commissioner, if he came to the conclusion that a corporation under his jurisdiction issuing securities was insolvent, or that the collaterals were getting in bad condition, that he could make an order referring the matter to the Attorney General of the State, and the Attorney General, under that statute, would have the right to take such action as the Attorney General wished to, [111] using the name of the State, as might be necessary, and could apply to the Circuit Court of the State for the appointment of a receiver.

I told Mr. Goodwin at the time that he should have the Corporation Commissioner make that order and refer it to our office, the Attorney Gen-

(Testimony of Ralph E. Moody.)

eral's office, and I would see what we could do about it.

Q. Let me ask: In what capacity was Mr. Goodwin?

A. He was Assistant Corporation Commissioner. I forget his title, but he was one of the assistants in the office of the Corporation Department.

So, then, that order was made, and I looked into the matter and, of course, we could not proceed in the State Court because they had filed a petition in Bankruptcy in the Federal Court.

I noticed that that petition had been filed in 1931 and that nothing had been done, no declaration of bankruptcy had been made by the Court, and they seemed to be operating just the same, and the creditors, the bondholders, were writing in, and they would get an answer that they could not do anything about it, that they were in bankruptcy.

Well, I had some little trouble figuring out what to do. The State was not a creditor. I knew something should be done, so I prepared a petition to the Federal Court and asked leave for the State of Oregon to intervene in that Bankruptcy [112] proceeding.

It was a kind of a novel proceeding. I found no precedent for it, but I knew if I could get in there and recite to the Court that the bankruptcy proceeding had been pending before the Bankruptcy Court for some three years and they were still operating and nothing being done, I knew that the Court would inquire into it.

(Testimony of Ralph E. Moody.)

I made that application to intervene—the petition, of course, was on file. I do not know whether you have it in the record in this case or not.

Q. Just a moment. We will find that petition. I hand you herewith pre-trial exhibit 155 and will ask you whether that is a copy of the petition you filed?

A. Yes. It was quite a long petition. That is it. I know I recited the history of the whole thing.

Q. I believe that there is a signature, Mr. Moody, as I recall.

A. I know. I dictated it.

Mr. Teiser: We will admit that that petition was filed.

Mr. Reilly: It is admitted. We offer the petition in evidence.

The Witness: Yes. I signed it in the name of Mr. VanWinkle and myself.

Mr. Teiser: If your Honor please, I object to the introduction in evidence of the intervening petition in bankruptcy, [113] unless it is introduced for the purpose of showing that the facts set forth in the complaint should have been discovered from it, and I take it that there is no such indication in that petition to that effect. I do not believe that the record of this case ought to be encumbered by the admission of this petition at this time.

The Court: The objection is overruled. Admitted.

(Intervening petition of the State of Oregon in re Western Bond and Mortgage Company, having been previously marked and identified as Defendant's Pre-Trial 155 was thereupon

(Testimony of Ralph E. Moody.)

received in evidence and marked Defendant's Exhibit No. 155.)

The Witness: Shall I continue?

The Court: No, just a moment.

Mr. Reilly: Q. Following the filing of that petition—first, did the Court permit you to intervene?

A. Yes, the hearing first was upon the granting of permission for me to intervene, and the Court permitted it, and that was resisted. I think Mr. Agnew, an attorney from Seattle——

Q. For the corporation, the Western Bond and Mortgage Company?

A. Yes. He came in and he resisted, and it was heard before Judge McNary, and Judge McNary permitted it.

Q. And at the same hearing was the question of the appointment of a receiver argued?

A. Yes. He heard it and took the matter under advisement for [114] some little while, as I remember, and then appointed Mr. George McBride.

Q. As receiver?

A. As receiver in the matter, and then the bankruptcy—I think that I had the bankruptcy meeting pressed so they were declared a bankrupt and then——

Q. I think you are ahead of your story, Mr. Moody. The corporation was not declared a bankrupt until December.

A. Well, I knew it was about that time.

Mr. Teiser: When was it declared bankrupt?

The Witness: So——

(Testimony of Ralph E. Moody.)

Mr. Teiser: I withdraw that.

Mr. Reilly: I guess it was November, wasn't it?

Mr. Teiser: I could switch you straight on that matter, if you care to. The petition was——

The Court: If we are going to have any conferences between counsel, I will leave the bench.

Mr. Teiser: If your Honor wants to know the facts, I can give them to you. I am sure that both of these gentlemen will agree to them. If it is not material in this regard, I will sit down.

Q. Well, following the appointment of Mr. McBride, as receiver, did you go to Mr. McBride and consult with Mr. McBride?

A. No, I did not, not until after he was appointed. I did not know whom Judge McNary was going to appoint. [115]

Q. You misunderstood me. After Mr. McBride was appointed——

A. Oh yes.

Q. Then, you went to see him?

A. Yes, I went to see Mr. McBride.

Q. What, if any, discussion did you have with him concerning Western Bond and Mortgage Company matters at that time?

A. Well, I went to see Mr. McBride and I told him that the state was interested, insofar as the state had a moral obligation, and so on, insofar as protecting the assets of this corporation, of the bankrupt corporation. The Attorney General's office also asked the Corporation Department to furnish them a list of all bond holders and creditors, and I dictated the form of the letter to be



(Testimony of Ralph E. Moody.)

sent to all of these bondholders, reciting what the state had done thus far, and I think I solicited them for their powers of attorney in the name of the Attorney General and told them about the United States Court appointing Mr. McBride.

Q. I have the letter here, Mr. Moody. I will ask you if Defendant's Pre-trial 156 is a printed and signed copy of the letter to which you refer?

A. Yes, I signed that letter.

Mr. Reilly: We offer the exhibit in evidence.

Mr. Teiser: I object to the introduction of the letter in evidence. It has no bearing; it is immaterial in this case, the letter soliciting claims of creditors, and has no [116] evidential value in this case.

The Court: Overruled. Admitted.

(Form of letter circulated by the office of the Attorney General, State of Oregon, to creditors of Western Bond and Mortgage Company, having previously been marked and identified as Defendant's Pre-trial 156, was thereupon received in evidence and marked Defendant's Exhibit 156.)

Mr. Reilly: Q. I also hand you defendant's pre-trial 157, and will ask you whether that was the proof of claim and power of attorney which accompanied the letter which you sent to all creditors? A. Yes, that looks like it.

Mr. Reilly: We offer the exhibit in evidence.

Mr. Teiser: Objected to on the same ground.

The Court: The same ruling.

(Testimony of Ralph E. Moody.)

(Form of proof of claim and power of attorney, accompanying Defendant's Exhibit 156 having previously been identified and marked as Defendant's Pre-trial 157, was thereupon received in evidence and marked Defendant's Exhibit 157.)

Mr. Reilly: Q. Then, to go on in a chronological order, what happened next?

A. Well, we received responses to these letters, and then we [117] attended at the meeting of the creditors in Mr. Cannon's office here, then the Referee in Bankruptcy, and Mr. McBride was selected as Trustee.

Q. During the time preceding the filing of your petition for intervention, in other words, during the time preceding July of 1934, was any auditor of the Corporation Department at work on the affairs of the Western Bond and Mortgage Company, other than Mr. Goodwin?

A. Well, Mr. Goodwin was working on the matter and assisting at the time was Alan Brown.

Q. Is that the Alan Brown who has recently been appointed a County Commissioner?

A. That is the Alan Brown who has recently been appointed County Commissioner of this county.

Q. And then, when you discussed this matter with Mr. McBride, following his appointment as receiver—did you have more than one meeting with him?

A. Oh, yes, I had several meetings with Mr. Mc-

(Testimony of Ralph E. Moody.)

Bride. I was quite interested in the matter and I came down here and conferred with him many times, with Mr. Goodwin and Mr. Brown also. He was given the assistance of the auditors and the clerical force of the Corporation Department.

Q. Did you have any conversation with him respecting any civil or criminal liability that might attach to Mr. Farrington in respect to any prosecutions? [118]

A. Well, I told him that he was to look into the matter very carefully and to collect all of the assets that were due.

The corporation had created a lot of subsidiary corporations, and I asked him to particularly look into that thing and to collect—to find out all of the assets that were due the company.

I remember at one particular time there was The Bank of California matter and I understand that since they have had some judgment.

Q. I want to direct your attention particularly—

A. Oh, yes. Then, as far as Mr. Farrington was concerned, I know I called Mr. McBride's attention to the fact, I think, that Mr. Farrington was interested in the original organization of the Western Bond and Mortgage Company, and the records showed that when they first made application to the corporation commissioner for a license to sell these securities he refused it, whereupon he proceeded to institute in the Circuit Court of the

(Testimony of Ralph E. Moody.)

state—to apply for a mandamus compelling the corporation commissioner to accept their filing.

Q. Who was the attorney for the Western Bond at that time?

A. I think Arthur Spencer. Then, there were other transactions in there that looked questionable between Ridgway and——

Q. ——Farrington?

A. And O'Flynn and all of them. As a matter of fact, the whole thing needed a very thorough investigation. [119]

Q. Did you have any discussion with him respecting the lawsuits that had been brought in 1931, charging Mr. Farrington with having defrauded the company?

A. Well, there were some articles published in the newspaper at that time. The newspapers gave a great deal of publicity to this whole business, this whole transaction, and I was watching it very closely, and whenever there was some reference to some proceeding about Mr. Farrington, that was called to Mr. McBride's attention.

Q. By you? A. Yes.

Q. What, if any offers of assistance, in the way of auditing assistance, or accounting assistance, if any, did you make to Mr. McBride?

A. Well, he was to get all of the assistance from the Corporation Department and get all the assistance that he required and Judge Carey, who was then Corporation Commissioner, had an office here in Portland, and they gave him assistance. Mr.

(Testimony of Ralph E. Moody.)

Goodwin, I think, was the main one and Alan Brown, and there were others, so he had all he wanted.

Q. What, if anything, was done as to the payment of a salary to him and expenses?

A. Well, I will explain about that. I really think that Judge McNary called my attention to the fact, when he told me that he had appointed Mr. McBride. He said there did not seem [120] to be much assets in the corporation, and he did not know how it could pay; they could not issue any receiver's certificates.

Anyway, I took the matter up with the Attorney General and the Corporation Commissioner, Judge Carey, and they agreed to pay Mr. McBride \$150 a month.

I heard Mr. McBride's testimony yesterday. I understood him to say that that came on a voucher from the Attorney General's office. He may be right about that, but I think that was paid on a voucher from the Corporation Department.

Q. Well, I do not know how important that is, but my impression is that one department paid a part and the other paid the other part.

A. I know that payment was made of \$150 a month, with the consent of the Attorney General, Mr. VanWinkle, and Judge Carey, who was Corporation Commissioner, and they continued that payment to him until some time after he was appointed Trustee. I do not remember how long. The records will show.

(Testimony of Ralph E. Moody.)

Mr. Reilly: In connection with the testimony of this witness, your Honor, we offer in evidence Defendant's Pre-trial 158. I assume there is no objection.

Mr. Teiser: Yes, I would object to the materiality of the voucher.

The Court: Well, you introduced testimony about it. The objection is overruled. [121]

(Voucher of the State of Oregon, in amount \$490.85—two pages—previously marked and identified as Defendant's Pre-Trial No. 158, thereupon received in evidence and marked Defendant's Exhibit No. 158.)

Mr. Reilly: I also offer in evidence, in the same connection, the voucher marked Defendant's Pre-Trial 160, showing payment up to June 13, 1935.

Mr. Teiser: I make the same objection.

The Court: The same ruling.

(Voucher of the State of Oregon, in amount \$900—three pages—previously marked and identified as Defendant's Pre-Trial 160, thereupon received in evidence and marked Defendant's Exhibit No. 160.)

Mr. Reilly: May I ask if it is admitted that these sums were received?

Mr. Teiser: Yes, it is admitted that those sums were received.

Mr. Reilly: No use encumbering the record with the checks, your Honor.

Q. Was any limitation placed by you on the pur-



(Testimony of Ralph E. Moody.)

poses for which the Corporation Department auditors could be used by Mr. McBride? A. No.

Q. What were your own statements to Mr. McBride in that connection, if you made any?

A. Just as Mr. McBride testified to yesterday upon the stand. [122] He was told that he would have the assistance of the Corporation Department, its auditors, and everything else that he might require, in order to make a thorough investigation of the affairs of this bankrupt concern.

Q. Do you know whether Arthur Spencer is still alive, still living?

A. He is dead. I know he is dead.

Q. Do you know when he died? If I stated to you, 1942, would that be about right?

A. Well, I would just be guessing at it. I know he is dead, but I do not know the year. I couldn't tell you.

Mr. Reilly: May we agree on that? I checked this morning and found it was May—I have forgotten whether it was the 12th or 18th—1942.

Mr. Teiser: I will admit that. I will agree that he died at the time you say, but I object to the materiality of it.

The Court: The objection is overruled.

Q. Is Judge Carey dead?

A. He is dead, too.

Mr. Teiser: That is admitted.

Mr. Reilly: I do not know the date.

Q. Do you know approximately how long ago he died? A. No, I don't know.

(Testimony of Ralph E. Moody.)

The Court: I do not know either, but it makes very little difference. [123]

Mr. Reilly: The only question would be whether or not he had some part in this transaction.

The Court: When did you want to prove that he was dead?

Mr. Reilly: Before the beginning of this suit.

Mr. Teiser: I would say he died before that time.

The Court: For the purposes of this case, can't you agree to it?

Mr. Teiser: Yes.

The Court: You say it is immaterial, but the Court overrules your objection. Go ahead.

Mr. Reilly: That is all.

### Cross-Examination

By Mr. Teiser:

Q. Mr. Moody, just for the purpose of testing your memory, to a certain extent, may I say to you, if you recall it, that you testified Mr. Agnew resisted the petition in bankruptcy?

A. Yes, he did.

Q. The intervening petition?

A. Yes, that is, he resisted the State's application to present its petition.

Q. Did he not consent to the adjudication in bankruptcy?

A. After the Court granted the State's right to intervene and appointed Mr. McBride as receiver, why, he may have consented. I do not know as to

(Testimony of Ralph E. Moody.)

that, but I know that the purpose of the proceeding was to press the bankruptcy proceedings. [124]

Q. You indicated that Mr. Agnew resisted the bankruptcy and I——

A. I misstated myself, then. What I meant to say was that Mr. Agnew resisted the filing of the petition.

Q. You spoke of some papers, some articles being published in the newspapers and, that you saw the articles because you were interested. That was in 1934 that you are speaking of, articles appearing in the papers of 1934, is that right?

A. In answer to that, I wanted to say that I was quite interested in the case. It was a live case for me, and it had been assigned to me, and there was considerable publicity about the State intervening, and there was also considerable publicity in regard to the Western Bond and Mortgage Company, and I instructed all of them that whenever any article appeared in the paper about that to call my attention to it and, while I do not mean to say that I have any independent recollection about reading any article, I know when ever I did I came to Portland and spent several days at a time, talking to Mr. McBride, and his attention was always called to these things.

Q. What I am speaking about is that you referred to newspaper articles published concerning matters which had occurred after you became interested in the bankruptcy proceedings.

A. Yes, after I became interested.

(Testimony of Ralph E. Moody.)

Q. And not before 1934?

A. I, myself, knew nothing about the Western Bond and Mortgage [125] Company until it was referred to me some time in 1934.

Mr. Teiser: That is all.

### Redirect Examination

By Mr. Reilly:

Mr. Reilly: In connection with the question just asked the witness——

The Court: What are you looking for?

Mr. Reilly: I beg your pardon?

The Court: What are you looking for?

Mr. Reilly: I am looking for some exhibit. We offer in evidence, if your Honor please, an article from the Oregonian of July 20, 1934, marked Defendant's Pre-Trial 79, which refers to the civil and criminal liability of Mr. Farrington.

Mr. Teiser: I object to the introduction of the exhibit, on the ground that it is not shown that it was brought to the attention of the Trustee, nor that it was read by him, nor that it is shown that it was exhibited by the witness to the receiver or Trustee.

The Court: Overruled. Admitted.

(Copy of article from the Oregonian of Friday, July 20, 1934, previously marked and identified as Defendant's Pre-Trial 79, was thereupon received in evidence and marked Defendant's Exhibit No. 79.)

(Testimony of Ralph E. Moody.)

The Court: Incidentally, the adjudication of the Western [126] Bond and Mortgage Company as a bankrupt was September 24, 1934, if it is of any interest to anybody.

Mr. Reilly: The Trustee was not elected until December?

The Court: I do not know anything about that. You asked about the date of the adjudication. That is the date of adjudication, if you want it in the record.

Mr. Reilly: Thank you.

Mr. Teiser: What date, your Honor?

The Court: September 24, 1934. Incidentally, there is another matter that I want cleared up, and we might as well do it now. That is that this court has already adjudicated that the Ochoco Farms is a subsidiary of Western, and the witness who was on the stand yesterday said it was not a subsidiary, that it was a subsidiary of Massachusetts Mortgage. Inasmuch as he has already gotten a pretty good fee, owing to the fact that it was a subsidiary, I do not think it lies in him to deny that it was not a subsidiary.

Mr. Teiser: If your Honor will recall, it was shown in the other case that Ochoco fees were paid for by the Western Bond and Mortgage Company, the fees for incorporation, but the stock, I think, was actually held by or supposed to be held by the Massachusetts Mortgage Company, although it was not definitely known whether it was held by the Massachusetts or the Western, but the stock itself

(Testimony of Ralph E. Moody.)

I think was written out, insofar as it could be then done, in the name of Massachusetts. I think that [127] was the situation, but I think it was held by your Honor that Ochoco was never——

The Court: Everybody has cashed in on the whole thing, so I do not think we are going to change it now. As a matter of fact, I know that the stock was issued to Massachusetts, but I made no reference to that in my opinion. I think it makes no difference. I think it was a subsidiary, still, of Western, because it was Western's own employees who organized it, it was Western's money that went to pay for the articles of incorporation, and actually, as a matter of fact, it never was organized.

Mr. Teiser: It never really was organized.

The Court: Never was really organized.

Mr. Reilly: We know nothing about it. That was after Mr. Farrington was out of the Western Bond. I do not know when this corporation was organized, but Mr. Farrington was not connected with Western Bond.

The Court: There is testimony in this record made yesterday by the accountant.

Mr. Reilly: Yes, I remember that, your Honor.

The Court: That is why I wanted it checked up in this record, that the Court does not think that there is any point to it at all, one way or the other. I want to announce my opinion right now, regardless of what has been said, that it was a subsidiary of Massachusetts.

Mr. Reilly: It is not clear to me that that comes



(Testimony of Ralph E. Moody.)

into [128] issue in any way in this proceeding, your Honor, as far as I know.

The Court: I do not think that it does.

Mr. Reilly: Yes.

The Court: But, on the other hand, why, the witness said so twice in his testimony.

Mr. Reilly: Very emphatically.

The Court: That it was a subsidiary of Massachusetts, and I want the record to show that the Court takes knowledge of the Court's opinion here in the record and that Court is not going to permit that testimony to stand unchallenged.

Mr. Teiser: The Court's opinion obviously was correct.

Mr. Reilly: In this same connection, we offer in evidence an article from the Oregonian of July 15, 1931, marked as Defendant's Pre-Trial 76.

Mr. Teiser: 1931?

Mr. Reilly: No, 1934.

Mr. Teiser: Not No. 76, is it?

Mr. Reilly: Have I the wrong one?

Mr. Teiser: Yes.

Mr. Reilly: I will withdraw that offer, your Honor. I am sorry.

I offer Defendant's Pre-Trial 78.

Mr. Teiser: I was under the impression that was just offered, your Honor. May I ask what exhibit was just offered, [129] previous to this last offer?

The Clerk: 79.

Mr. Teiser: I make the same objection.

(Testimony of Ralph E. Moody.)

The Court: The same ruling.

(Copy of article from the Oregon Journal of July 19, 1934, heretofore marked and identified as Defendant's Pre-Trial 78, was thereupon received in evidence and marked Defendant's Exhibit No. 78.)

Mr. Reilly: I offer in this same connection Defendant's Pre-Trial 80, which consists of two articles from the Journal one of August 4, 1934, and the other, August 13, 1934.

Mr. Teiser: I make the same objection, if your Honor please.

The Court: The same ruling.

(Article from Oregon Journal, Saturday, August 4, 1934, and article from the Oregon Journal of Monday, August 13, 1934, previously marked and identified as Defendant's Pre-Trial 80, thereupon received in evidence and marked Defendant's Exhibit No. 80.)

Mr. Reilly: We next offer in evidence Defendant's Pre-Trial 81, being an article from the Oregon Journal dated August 14, 1934.

Mr. Teiser: The same objection, if your Honor please.

The Court: The same ruling.

(Copy of article from Oregon Journal of August 14, 1934, previously marked and identified as Defendant's Pre-Trial 81, thereupon received [130] in evidence and marked Defendant's Exhibit No. 81.)

(Testimony of Ralph E. Moody.)

Mr. Reilly: We next offer in evidence Defendant's Pre-Trial 83, being an article from the Oregonian of August 14, 1934.

Mr. Teiser: The same objection.

The Court: Same ruling.

(Copy of article from the Oregonian of August 14, 1934, previously marked and identified as Defendant's Pre-Trial 83, thereupon received in evidence and marked Defendant's Exhibit No. 83.)

Mr. Reilly: That is all.

(Witness excused.)

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## JOHN R. LATOURETTE

was thereupon produced as a witness on behalf of the defendant and, being first duly sworn, was examined and testified as follows:

### Direct Examination

By Mr. Reilly:

Q. Mr. Latourette, you are an attorney at law, practicing your profession in the State of Oregon?

A. Yes.

Q. And your offices are here in Portland?

A. Yes.

Q. How long have you been a member of the Bar of the State of Oregon, Mr. Latourette?

A. Since 1908.

(Testimony of John R. Latourette.)

Q. And you are a member of the Bar of this Court?      A. Yes.

Q. And of other Federal Courts?

A. Well, I don't know.

Q. Were you, in any way connected with the bankruptcy proceedings of the Western Bond and Mortgage Company, bankrupt, at any time?

A. I was the attorney of the Trustee at a time.

Q. From what time to what time?

A. Well, I don't know as I can answer that. It was a long time ago.

Mr. Teiser: If your Honor please, if it will help counsel, I will admit that Mr. Latourette was attorney for the Trustee [132] from the time the Trustee qualified, or shortly thereafter, until he withdrew and I took over the case as attorney for the Trustee.

The Witness: I think probably about a year.

Mr. Reilly: Well, we will offer in connection with this testimony Defendant's Pre-Trial 104, being a copy of the order authorizing Mr. Latourette's employment as attorney, dated March 28—filed March 28, 1935.

The Court: Admitted.

(Copy of order authorizing Trustee to retain attorney in matter of Western Bond and Mortgage Company, bankrupt, No. B-16772, in the District Court of the United States for the District of Oregon, previously marked and identified as Defendant's Pre-Trial 104, thereupon

(Testimony of John R. Latourette.)

received in evidence and marked Defendant's Exhibit No. 104.)

Mr. Teiser: No objection.

Mr. Reilly: Q. Mr. Latourette, so that no question of privilege will come up, I will ask you about what knowledge, if any, you had of Western Bond and Mortgage Company matters, or prior litigation, before you were employed as counsel for the Trustee? A. What knowledge?

Q. Yes. A. I don't think I had any. [133]

Q. The questions from now on I think are subject to a claim of privilege. Mr. Latourette, following your employment, did you make any investigation of Western Bond and Mortgage Company matters? A. I did.

Q. What investigations?

Mr. Teiser: Just a second. That will be up to counsel to determine whether he wants to claim privilege.

Mr. Reilly: We will go along and see where we get.

Q. What investigations did you make, Mr. Latourette?

The Witness: Do I have to answer that question, your Honor?

The Court: Are you claiming privilege?

The Witness: I assume it is up to the client to make that claim, is it not?

Mr. Reilly: That would be my understanding.

Mr. Teiser: We hesitate to make such a claim, your Honor, because that attempt puts us in a po-

(Testimony of John R. Latourette.)

sition that we want to hide something. We have taken the position that we have nothing to hide and, so, I hesitate to make the claim.

The Court: I am inclined to think you would have to affirmatively waive it. If not, it is all right for Mr. Latourette to go ahead and testify. I think the obligation is on you. If you want to release him, all right; if you do not want to release him why, say so. It is a question I [134] think your client has to decide.

Mr. Reilly: Yes.

Mr. Teiser: I will discuss it with my client, your Honor.

The Court: Take a short recess.

(Recess.)

Mr. Teiser: So the record may be clear, the Trustee waives the question of privilege on the part of counsel.

Mr. Reilly: Q. Mr. Latourette, what were the things you investigated?

A. When I was appointed and Mr. Cannon was Referee, he told me that Mr. Moody of the Corporation Department had been through this, and to get in touch with him and to collaborate with Mr. Moody, which I did.

Q. I do not care about all of the things you investigated, but what, if any, investigation, did you make concerning Mr. Farrington?

A. Well, we investigated everybody we could from the time I was in there, trying to get some assets. We investigated Mr. Farrington, the Bank



(Testimony of John R. Latourette.)

of California—we had two accountants from the Corporation Department that were in my office a number of times and were in Mr. McBride's office. I was down there. I went through as many records as I could find that pertained to any of the people that were involved in the thing.

I think I was in there for about a year and we [135] concluded that we had a case against The Bank of California, and I prepared a complaint, a rough draft, which I was waiting to submit to Mr. Moody for his approval. I never got to see Mr. Moody or never prepared the complaint in its final form during the time I was representing the Trustee, I think about a year or more.

Q. What, if anything, did you discover about any lawsuits which had been brought concerning the Western Bond and Mortgage Company and Mr. Farrington in 1931?

A. I do not recall anything about that except I know that there had been some lawsuits brought.

Q. What, if any, discussion did you have with Mr. McBride, the receiver, concerning those suits and the matters therein alleged?

A. I don't know. I can't say definitely that I had any particular discussion with Mr. McBride about the particular suits. I know they were trying—we were trying to find out about the whole thing, about Mr. Farrington, as well as all of the others who had been involved in the thing, but as to any particular conversation regarding those things after these, so many, years, I do not recall.

(Testimony of John R. Latourette.)

Q. What about these auditors to what extent were you given a free hand?

A. In using them?

Q. The State Department's auditors? [136]

A. Mr. Moody told them to cooperate with us, and they were available to us at all times, and they had been through the records pretty thoroughly. It seems to me that they had made a pretty general report. I might be mistaken about that, though.

Q. Prior to your ceasing to be the attorney for the Trustee, you had drawn a rough draft of the complaint for the Trustee against the Bank of California?

A. Yes, I had.

Q. Arising out of the Russell ranch transaction?

A. I think that is what it was. It was some \$280,000 deal, as I recall it. I had that drawn for some little time. It was a typewritten draft with some pencil changes I had made.

Q. Do you still have that?

A. Yes, I do. There was some question as to whether we should proceed in the State Court or the Federal Court, and we had drawn the complaint in the State Court. I was not satisfied with the situation and I wanted to talk to Mr. Moody about it.

Q. Was the Keystone Finance Company mixed up somewhat in that lawsuit in connection with which you had drafted your complaint? Do you recall that name?

A. I recall the name. It seems to me it was some subsidiary, either of the Mortgage Company or The

(Testimony of John R. Latourette.)

Bank of California, I have forgotten. Some title, I believe, involved. [137]

Q. What was the nature of the action that you were proposing to prosecute against the Bank of California? Was it a preference or conversion?

A. I think for preference. They had borrowed money from the bank and the bank had taken, as I recall, a farm or something in Eastern Oregon or Eastern Washington, and we were trying to get that back.

Mr. Reilly: You may cross-examine.

Mr. Teiser: No questions.

(Witness excused.)

Mr. Reilly: I will call Mr. Teiser. I dislike doing so, but it is necessary in this case, your Honor.

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### SIDNEY TEISER

was thereupon produced as a witness on behalf of the defendant and, being first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Reilly:

Q. I hand you herewith Defendant's Pre-Trial 107, being a petition for the approval of an agreement between yourself and the Trustee. You are the attorney for the Trustee in this case?

A. Yes, sir.

(Testimony of Sidney Teiser.)

Q. And have been since 1936?

A. I think that was the year, sir.

Q. I have a copy of the petition for your appointment, dated June 10, 1936. A. Yes.

Q. That, you would say, was correct?

A. That is right. I assume so.

Q. Now, Mr. Teiser, referring to paragraph 1 of that petition for the approval of an agreement between yourself and the Trustee as to fees, there occurs the following statement concerning which I wish to interrogate you:

That after the employment of said attorneys, said attorneys made a study of the various documents, books and papers of the Bankrupt and of various transactions which had occurred between the Bankrupt and others, which examination [139] extended over a period of many months; that his attorneys reported to him that there were certain matters and transactions in connection with the affairs of said Bankrupt out of which recovery might be had if diligently prosecuted.

What were those other matters that you had then discovered?

A. What were the other matters?

Q. The matters referred to in that paragraph that you had discovered at the date that this petition was verified, the 14th day of April, 1936?

A. Well, as I recall, this was a petition that—if I am not mistaken, it was a petition for the purpose of bringing suit against The Bank of California, was it not?

(Testimony of Sidney Teiser.)

Q. Well, you are the one to say what an instrument you drew said. Let me ask you this: You had not discovered the bank situation; that had already been discovered prior to your employment?

A. No, it had not, as far as I know—I do not know what you mean by “discover.” The fact was that The Bank of California deal stuck out like a sore thumb throughout the entire records of the case up to the time I came into it, but nothing was being done about it, and we investigated that situation. I investigated it, because I could not understand why something had not been done about it and, because nothing had been done about it, I caused a more thorough examination to be made, thinking that there was something behind it that I did not know. [140]

After it had been done, we went to the Referee and presented the matter to him verbally, and in this petition and, as I recall, also the Besson and Brown situation that we felt should be litigated.

I think also there was another situation that arose in regard to some transfer of property down in Coquille, or down in Corvallis, somewhere in that part of the state. Those were things that we discovered and discovered at that time.

Q. And those were all the things that you are or were referring to in your petition for the approval of a contingent fee contract with yourself?

A. Well, as far as I recall, I took up with them the petition for an allowance of fees in handling the matters, which was to go to the creditors for

(Testimony of Sidney Teiser.)

their approval and which did go to the creditors at their meeting—covered not only things that we had ascertained then but things which we might ascertain, so that we might have authority for prosecuting them thereafter.

Mr. Reilly: We will offer the document in evidence as bearing on some further inquiry that we want to make.

Mr. Teiser: I have no objection to the offer, speaking as an attorney. I have no objection to the offer of the document to show that some investigations were made in regard to some things. If it is offered for the purpose of showing [141] that we handled the matter for a fee, or as to any details of the fee, I think it is immaterial.

The Court: Admitted.

(Copy of petition for approval of agreement, filed April 16, 1937, heretofore marked and identified as Defendant's Pre-Trial 107, was thereupon received in evidence and marked Defendant's Exhibit No. 107.)

Q. An order was made approving that agreement?

A. On that petition, if I recall rightly, a meeting of the creditors was called and the matter presented to the creditors and passed on by the creditors, and after the creditors' meeting was held and this was passed on by them, I think the Referee then approved the order.

Q. I mean, the order was approved?



(Testimony of Sidney Teiser.)

A. The order was made.

Q. The agreement was approved?

A. Well, an order was made for us to handle the cases which might arise at a stipulated fee, to be approved by the Referee, but the creditors consented to that agreement.

Q. Now, at that time, did you or did you not know of the litigation that had been brought in 1931, notably the case of Brockie against the Western Bond and Mortgage Company and C. H. Farrington and others, in this court, and the case of Pape and others against the Western Bond and Mortgage Company, [142] and others, in the Circuit Court of Multnomah County, and the case of Thompson against the Western Bond and Mortgage Company, and others, in the Circuit Court for Multnomah County?

A. I knew of a case of Thompson, or I think that was the case that Allen McCurtain brought.

I saw Allen McCurtain on the street one day—I don't recall whether it was before this time or afterwards, but some time when we contemplated litigation or had just brought litigation in regard to The Bank of California transaction. Allen McCurtain told me that he had been in this case at one time in an endeavor to get a receiver appointed in the State Court, and that he just could not get anywhere with it; that he hoped I would be successful. That is the only data I had. As far as I know, I did not have a complaint and did not particularly know anything about it, except his

(Testimony of Sidney Teiser.)

word that it was a suit for a receivership because of the insolvency of the company.

Q. The suit to which you refer was that of Thompson against the Western Bond and Mortgage Company and I will hand you——

A. If that was the suit.

Q. I will hand you Defendant's Pre-Trial 86, so that you may check that to see if that was the suit Allen McCurtain brought.

A. I knew about it. What is more, I knew it was brought into question during the litigation before the Referee. Yes, this is the complaint signed by Allen McCurtain. I take it this is [143] what he was referring to.

Mr. Reilly: We will offer the document in evidence.

The Witness: I do not recall ever seeing this complaint.

The Court: Admitted.

(Copy of amended complaint in H. C. Thompson, et al., versus the Western Bond and Mortgage Company, et al., in the Circuit Court of Oregon for Multnomah County, heretofore marked and identified as Defendant's Pre-Trial 86, was thereupon received in evidence and marked Defendant's Exhibit No. 86.)

The Witness: I was saying that as I recall in other litigation before the Referee some questions were asked, or cross questions indulged in, in which the suit of Thompson against the Western Bond

(Testimony of Sidney Teiser.)

and Mortgage Company, and perhaps others, was mentioned in that litigation, but I did not, as far as I know, make any investigation of those complaints. I knew that they were not successful. So far as Allen McCurtain's complaint was concerned, that is the Thompson complaint, I was told that it was a suit for a receivership, based on insolvency and impropriety, but I made no investigation of it. I do not think it was necessary or called for. I do not think as it stands now—perhaps I should not testify about what I think.

Q. I do not mind. [144]

A. I want to be fair.

Q. You did not, at that time, know that the litigation brought by Pape and others——

A. At what time?

Q. At the same time you knew of the McCurtain suit, shortly after your employment as attorney?

A. Let me say this: To the best of my memory I heard—Allen McCurtain told me about this suit that he brought, and that was the first I knew about any suits being brought against the Western Bond and Mortgage Company in connection with the receivership; but, then, when we got into the litigation and were trying the Bank of California case before the Referee, I think both Referee Snedecor and Referee Cannon, in one or both of these instances, of these trials, some of these cases were mentioned. I do not know whether the Brockie case was or not, but I am inclined to believe it was mentioned by name.

(Testimony of Sidney Teiser.)

Q. Now, you have read the record and you know perfectly well it was, do you not? A. Sir?

Q. You have read this record and you know perfectly well it was?

A. I don't know at this moment, no. I have given you the best testimony I could. If you say it is in there, I would say it was. My recollection is that it was. If I knew perfectly [145] well it was, I would have said so.

Q. I will ask you if you interrogated the witness Thomas G. Greene as follows and if he made the following answers, in the trial of the case of George McBride, Trustee, against The Bank of California.

I am referring to Plaintiff's Pre-Trial 103, at Page 403 and Page 404. I will read the whole thing, unless you want me to stop, to interject something. This is from the cross examination by Mr. Teiser.

"Q. You say you went up to the court to hear these lawsuits?

"A. I did not hear any of the suits. I heard arguments.

"Q. Did you examine the papers in the case at all?

"A. Some I did, I read the petition in intervention, and one of the later petitions filed by Mr. Mott on behalf of the corporation commissioner in August of 1934.

"Q. That was long after?

"A. It had nothing to do with it at all.

"Q. But before this last move was made you

(Testimony of Sidney Teiser.)

heard the arguments, and I think you said one in the State Court?

"A. In Judge Hall Lusk's department and also before Judge McNary.

"The Court: When were these suits you refer to?

"A. One was commenced in March 1931 and the other one in April 1931, the principal one I think. There were four [146] or five others.

"Q. Did you see the complaints in these cases?

"A. No, only just to see who the parties were.

"Q. You heard the argument but didn't look up the complaints?

"A. Yes.

"Q. Why did you go up to hear the arguments?

"A. I knew it was the company in which O'Flynn was interested.

"Q. Why did you go? Why was that?

"A. Because the Bank of California was trying to get some additional security from the Western Bond and Mortgage Company.

"Q. Did you know of this suit against the Western Bond and Mortgage Company brought by Allen McCurtain?

"A. Yes, that was one of them.

"Q. And another brought by Carl Little?

"A. Yes.

"Q. And the John Brocker——"

That should be "Brockie".

"Q. And the John Brocker suit brought in the United States District Court?

(Testimony of Sidney Teiser.)

“A. Yes.

“Q. Colonel Clark was engaged in this suit, was he not? [147]

“A. There were eight or ten lawyers participating in that argument.”

The suit that you refer to as being the one Colonel Clark participated in was the Brockie case, was it not?

A. Colonel Clark brought the Brockie case, was the attorney in the Brockie case. I saw that from your exhibits, your pre-trial exhibits.

Mr. Reilly: I think it may be agreed that this testimony was taken beginning November 9, 1936, either on that date or within a very few days thereafter.

Mr. Teiser: Whatever date it shows.

Mr. Reilly: The record shows that “On November 9, 1936, at ten o’clock in the forenoon, the above-entitled cause came on for hearing before the Honorable A. M. Cannon, Referee in Bankruptcy, upon an order to show cause directed to the Bank of California.”

Q. Did you ask the questions that I have read to you as having been asked of Thomas G. Greene?

A. Undoubtedly.

Q. Yes.

A. May I go on and explain my purpose in asking them?

Q. I am not interested in that. I want merely to disclose right now the fact that they were asked.

Mr. Reilly: We offer in evidence Defendant’s



(Testimony of Sidney Teiser.)

Pre-Trial 62, which is a copy of the complaint in the case of John Brockie [148] against the Western Bond and Mortgage Company, and others, in the United States District Court.

Mr. Teiser: I object to it as immaterial, if your Honor please.

The Court: The objection is overruled. Admitted.

(Copy of complaint in the case of John Brockie versus Western Bond and Mortgage Company, et al., previously marked and identified as Defendant's Pre-Trial No. 62, thereupon received into evidence and marked Defendant's Exhibit No. 62.)

Q. I will ask you whether or not, at the same trial, the Bank of California case, before the Referee in Bankruptcy, in November 1936, the following occurred, Thomas G. Greene being on the witness stand and being interrogated on the cross examination by Mr. Thompson:

"Q. You may now answer the question; read the question.

"Question read as follows: 'Just tell what proceedings you heard, what was done, and what the Court's ruling was on the matter.'

"A. Yes. There was a suit commenced in the State Circuit Court in the spring of 1931 by a man who claimed to be the holder of certain installment certificates secured by mortgage trust indenture or indentures of the Western Bond and Mortgage Company. [149]

(Testimony of Sidney Teiser.)

“Mr. Teiser: I would like to object now to any testimony about any proceedings in the Circuit Court or any court unless the records of court are introduced. I do not think that would be admissible in this proceeding, it would have no bearing here. But I certainly object to his proceeding along that line unless the records are produced, which would be the best evidence of what took place.

“The Court: The testimony may be heard subject to the objection.

“A. It is my intention not to rely on the records or put that in evidence, but to tell what I knew and heard in court. I heard the argument in court and charges made as to the various fraudulent transactions; the receivership was denied, and the court said there had not been sufficient showing made against the Western Bond and Mortgage Company to justify the court to take the management of the corporation out of the hands of its officers and directors. Then again, another suit on the equity of these installment certificates in which attempt was made to effect a receivership. I heard the arguments there by more than half a dozen leading counsel in Portland, Oregon, and Judge McNary's decision, which was in effect the same as before, that mismanagement of the affairs of the Western Bond and Mortgage Company had not been shown sufficiently to justify taking the management out of the hands of its officers, and he denied the receivership.” [150]

Did that testimony and that colloquy take place?

(Testimony of Sidney Teiser.)

A. Undoubtedly.

Q. Mr. Greene's memory was faulty, of course, because as you know the Brockie case was dismissed, is that right?

A. I do not know whether he was referring to the Brockie case or not. I know that that case was dismissed, but I won't say his memory was faulty. I do not know whether it was or not. If he is human, it probably was.

Q. The Brockie case was filed in March 1931. I show you Defendant's Pre-Trial 108 and I will ask you if that purports to be the examination of witnesses in the matter of the Western Bond and Mortgage Company, Bankrupt, and will ask you if the following occurred as stated in the exhibit——

A. You want to ask me what?

Q. If that is correct?

A. You want me to read this?

Q. If you care to.

Mr. Reilly: Does your Honor intend to go right on through until we finish this? I think we can finish by one o'clock.

The Court: No, until half past twelve.

A. Mr. Reilly, I do not recall the exact language here, but I think on the pre-trial I admitted that the testimony was as set forth here.

Q. Yes.

A. This is a copy of the transcript. [151]

Q. This is copied from the deposition on file in the Referee's office.

(Testimony of Sidney Teiser.)

A. Yes. Well, I take it this pre-trial exhibit must have been admitted.

Q. That is correct.

A. I don't know—I just cannot say. I don't know whether that is the examination that occurred there or not. However, I won't question it.

Q. He, of course, produced the original record, and I think there was an admission to that effect and, while I myself did not do the copying, it was copied and compared.

A. I am willing to admit that that testimony was given, that the questions were asked and the answers given by me—the questions asked by and the answers given by the witness, subject to correction, if it is found that the original testimony shows otherwise.

Mr. Reilly: We will offer the exhibit in evidence, your Honor.

The Court: Admitted.

(Copy of examination of witnesses under Section 21-A, filed May 17, 1937, containing excerpts from the testimony of William G. Brown and Dr. John H. Besson, previously marked and identified as Defendant's Pre-Trial 108, was thereupon received in evidence and marked Defendant's Exhibit No. 108.)

Mr. Reilly: I want to have it, please. I want to ask some more questions concerning it.

Q. The first deposition was that of William G. Brown, taken on the 18th day of February, 1937 and, in connection with the taking of that deposi-

(Testimony of Sidney Teiser.)

tion, were the following questions asked by you and the following answers given:

“Q. You are familiar with the Oregonian, a Portland newspaper?

“A. Oh, yes.

“Q. Read it every day?

“A. Well, yes, I would say so. I always do so when I have been here.

“Q. I show you some articles from the Oregonian. Do you remember reading them or seeing them?

“A. What is the date of that?

“Q. 1931.”

Then, further down:

“Q. You did not know anything about that matter from the early part of the year 1931 down to the latter part of that year?

“A. Nothing.”

What were those newspaper articles appearing in the Oregonian that you handed to the witness?

A. As I recall the articles—and I am rather positive about this—they were exhibits that were introduced in the Bank of [153] California case from the file of the Bank of California. The Bank of California had a credit file, and in this credit file they had data concerning the Western Bond and Mortgage Company for quite a period of time, and among them were newspaper articles or clippings, and the clippings were to the effect that the Western Bond and Mortgage Company were declared not subject to receivership because they

(Testimony of Sidney Teiser.)

were not insolvent or because they were properly handling their affairs.

My purpose in asking those questions——

Q. I am not interested in your purpose. I am interested only in your knowledge.

A. I think it would have a lot to do with it.

Q. Perhaps, but it makes no difference to me.

A. Well I want to state my purpose.

Mr. Reilly: I object to any argument in support of his purpose in asking the questions and the purpose of the inquiry relates only to his knowledge.

A. My purpose——

Mr. Reilly: I think he is not answering the question, your Honor. That is part of my objection.

The Court: Answer the question.

The Witness: Shall I go ahead, your Honor?

The Court: Answer the question. I do not want you to answer something else. You are under examination now, Mr. Teiser. You are not an attorney in the case; you are answering questions. [154]

Q. I think you had finished answering my question. You may cross-examine yourself later.

Mr. Teiser: I will handle it that way so that there will be no controversy.

Q. On that same day, now, which was February 18, 1937, in the examination of John H. Beson, did the following occur, questions by you:

“Q. The newspaper items and articles in the early part of 1931 about the receivership and finan-



(Testimony of Sidney Teiser.)

cial difficulties of the Western Bond and Mortgage Company appearing in the Oregonian and other Portland papers, did you notice them?"

Did you ask that question?

A. Undoubtedly.

Q. What were the newspaper articles you were referring to in the early part of 1931?

A. It was whatever newspaper clippings that were contained in the file of the Bank of California credit file, which was introduced—it was brought up to the Bankruptcy Court here by the Bank of California in the case of McBride, Trustee, against the Bank of California. They were used in the Besson case, or that file was used and these newspaper clippings were, as I recall, newspaper clippings concerning the receivership petitions that had been filed.

Mr. Reilly: Just a moment. We have some newspaper articles here which I would like to put in evidence. Your Honor, I [155] have here copies of all of the newspaper articles that a search could reveal in 1931 concerning the Western Bond and Mortgage Company matters. The first ones started in March and during the month of March. They next appeared in July, I think. I have not brought the girl here who typed them for me, but I could, if necessary, but we offer these three articles appearing in the Oregonian and the Journal, Telegram and Oregonian, March 13th, March 13th and March 14th, 1931, respectively.

First we offer the article which appeared in the

(Testimony of Sidney Teiser.)

Oregonian or, the Journal, rather, which is Defendant's Pre-Trial 63.

Mr. Teiser: I would object to the materiality of it, if your Honor please. As I say, it contains no information of itself of the character which you indicate and, secondly, because, so far as I know, anybody seeing any such articles in this manner——

The Court: The objection is overruled. I might explain to you that I do not think it makes any difference what you knew if, being charged with this duty to investigate and to bring an action, there was at hand information which pointed fairly directly to this matter; and that is the basis on which I am considering the materiality.

Mr. Teiser: I think that is the proper basis, your Honor.

(Copy of article from Oregon Journal of March 13, 1931, [156] previously marked and identified as Defendant's Pre-Trial 63, was thereupon received in evidence and marked Defendant's Exhibit No. 63.)

Mr. Reilly: We next offer Defendant's Pre-Trial No. 64. You have seen this?

Mr. Teiser: Yes, I have seen that.

Mr. Reilly: Is there any use of my submitting them to you each time?

Mr. Teiser: No, sir, not if you are not going to ask me any question about them.

Mr. Reilly: No.

Mr. Teiser: I make the same objection, your Honor.

(Testimony of Sidney Teiser.)

The Court: The ruling is the same.

(Copy of article from Portland Telegram of March 13, 1931, previously marked and identified as Defendant's Pre-Trial No. 64, thereupon received in evidence and marked Defendant's Exhibit No. 64.)

Mr. Reilly: I next offer Defendant's Pre-Trial No. 65.

The Court: The Court will receive this, subject to the same objection.

(Copy of article from the Oregonian of March 14, 1931, previously marked and identified as Defendant's Pre-Trial No. 65, thereupon received in evidence and marked Defendant's [157] Exhibit No. 5.)

The Court: At this time the Court is going to suspend until two o'clock.

(Thereupon at 12:30 P.M. a recess was taken until 2:00 o'clock P.M.) [158]

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Court reconvened at 2:00 o'clock P.M., Wednesday, November 29, 1944, pursuant to recess.

Mr. Reilly: In offering these exhibits, I do not know that there is any occasion for Mr. Teiser being on the witness stand. However, we might let him cross-examine himself now, if he so desires, and then offer the documents later.

The Court: Whatever order you wish to follow.

(Testimony of Sidney Teiser.)

Mr. Teiser: It is kind of a *normal* procedure, but I suppose it will have to be done.

The Court: All right. I think the method to pursue is to ask yourself questions and then give your answers.

Mr. Teiser: I am afraid so.

### SIDNEY TEISER,

having heretofore been duly sworn as a witness on behalf of the defendant, resumed the stand and further testified as follows:

### Cross Examination

By Mr. Teiser:

Q. If you had any copies of newspaper articles for the year 1931, concerning which you were questioning the witnesses Besson and Brown, in the proceedings against those two men, how did you obtain those articles?

Mr. Reilly: Object to that.

A. They were obtained during the process of the suit against [159] the Bank of California. We were endeavoring——

Mr. Reilly: That is not responsive to the question. I object because the witness is not answering his own question.

The Court: I think he is.

Mr. Teiser: I think so.

The Court: Go ahead.

A. We were endeavoring to bring home to the

(Testimony of Sidney Teiser.)

Bank of California knowledge of the fact that the Western Bond and Mortgage Company were insolvent and had a petition in bankruptcy filed against it and we called for their credit file.

There was an adjournment of court had and the Bank of California brought a file, which was a letter sized folder, in which there were letters, credit reports from Bradstreet or Dun, memoranda which they had made, and certain newspaper articles. Just what articles they were, or how many, I do not recall, but there were some newspaper articles in the file, along with these other matters. They presented them, and we questioned the officers of the Bank and its attorney concerning the facts in that file.

Now, when the——

Mr. Reilly: Have you finished your answer to that question?

The Witness: Yes.

Mr. Reilly: All right.

Mr. Teiser: I want to be fair about it.

Q. Was it after you came in possession of or had those newspaper [160] articles when you questioned Mr. Brown and Dr. Besson?

A. Well, it was necessary in that case likewise to show that Besson and Brown, or either or both of them, had knowledge at the time they received certain monies or assets from the Western Bond and Mortgage Company of the insolvency of the Western Bond and Mortgage Company, and for that purpose I obtained the exhibit which was introduced in the case of the Western Bond and

(Testimony of Sidney Teiser.)

Mortgage Company, and which was the credit file, and questioned Dr. Besson and Mr. Brown concerning the newspaper articles, which I recall contained only data concerning the insolvency or the alleged insolvency of the Western Bond and Mortgage Company, and that is, as I recall, what the newspaper articles were in reference to, what I was asking about.

Q. Did you see any newspaper articles at that time, or previous thereto, or at any time prior to the bringing of this suit, which had data in them relating to the facts set forth in the complaint, or matters connected therewith?

Mr. Reilly: That is objected to as calling for a conclusion of the witness. That question calls for a matter of opinion and not the testimony of any fact.

The Court: I think the witness intends to testify to facts. I will permit him to answer.

A. No, I saw no newspaper articles at any time except the newspaper articles that were in the file, which I referred to, and those newspaper articles certainly did not bring to my mind any [161] knowledge or have in them any information in any way relating to the matters as set forth in this complaint, or leading to information concerning those facts.

Mr. Reilly: Is that all?

Mr. Teiser: I am through, sir.



(Testimony of Sidney Teiser.)

Redirect Examination

By Mr. Reilly:

Q. Are the newspaper articles you saw the ones that are now in evidence?

A. I certainly would not know. In fact I have not read the newspaper articles that you handed in evidence, later than the time you presented them on pre-trial, but I would say that they were not the same articles—at least some of them are not the same articles that were in the Bank of California file.

Q. Are you able to point to any article in the papers in Portland in the early part of 1931, referring to any possible insolvency of the Western Bond and Mortgage Company, other than the newspaper articles relating to the Brockie case?

A. You mean these here?

Q. Anywhere. Do you know of any articles in any paper in the City of Portland referring to the question of the insolvency of the Western Bond and Mortgage Company, printed in 1931, early in 1931, before the first of July, except those articles relating to the Brockie case? [162]

A. I do not know of any newspaper articles at all. The only newspaper articles that I recall at all were the articles that I referred to as being the ones in the bank of California file, and I know those are the only newspaper articles that I saw, and these articles I know had to do with the insolvency of the Western Bond and Mortgage Com-

(Testimony of Sidney Teiser.)

pany, because that was the only purpose I could have asked concerning them. That was the issue.

Q. The petition in bankruptcy was filed November 25, 1931, is that correct?

A. I think that is the stipulation that we made.

Q. You do not call that the early part of the year, do you?     A. No, I would not.

Q. No?

A. I was not speaking about the bankruptcy now. I was speaking about insolvency.

Q. What were the articles about insolvency?

A. I have not the slightest idea. All I know is that whatever newspaper articles were in the file, the credit file of the Bank of California, were based on data—that had data in them concerning the insolvency of the Western Bond and Mortgage Company and asking for a receivership.

Q. Did you have in your hand, when you questioned the witnesses, the newspaper articles printed in the early part of 1931?

A. I would only judge that I must have had that file and that in that file must have been newspaper articles in 1931, because [163] the question was relative to that, but I would not have any independent memory.

Q. Please just answer my question. Did you have in your hand any item, or did you have in your hand, when you questioned these witnesses, any newspaper items and articles in the early part of 1931 about the receivership and financial difficulties of the Western Bond and Mortgage Com-

(Testimony of Sidney Teiser.)

pany, appearing in the Oregonian and other Portland papers? Did you have them in your hand?

A. I must have had it in the file, if I referred to that in that testimony.

Q. If you identified it from the newspaper, how did you discover that there was a case such as the Brockie case which was referred to in the cross-examination of Tom Greene, and the Pape case brought by Mr. Little, to which you referred in the same cross-examination? You have already explained the Thompson case, from having a talk with Allen McCurtain. How do you explain your knowing there were any such cases except from the newspapers?

A. My recollection about the matter was that the matter was first brought out by Mr. Thompson when he was questioning Mr. Greene in regard to these newspaper articles and—or, anyhow, these suits, and, naturally, I inquired about them, or, if not that, from some other questioning that arose in that case, because I had no knowledge, I know, about any Brockie suit; in [164] fact, as I recall it, I even miscalled the name, when I questioned him about it.

Q. You miscalled it or the reporter did not get it right?

A. I don't know. It is wrong in there.

Q. I will ask you if, as a matter of fact, you did not bring that matter out yourself in the direct examination of Tom Greene, as a part of the first part of your case?

(Testimony of Sidney Teiser.)

A. No, I do not think so. I do not think that I first questioned Mr. Greene, although, of course, I can be mistaken as to that. It has been seven or eight years ago, six or seven years ago. You have got the record there. I haven't it before me, but I know that the only case I knew that had been brought——

Q. I will take that back, Mr. Teiser. What you asked about was his knowledge of——

A. ——the Thompson case?

Q. No. You did not name the cases then but you did name them later.

A. I am sure, Mr. Reilly, I had no knowledge of those cases until they were brought out by Mr. Greene through the questioning by Mr. Thompson, or otherwise, because if I had any knowledge before that time of those suits I am quite sure that I would have remembered it.

Q. Are you familiar enough with this record now so you think you could point out wherein the names of those cases came into the case except by your own interrogation on cross-examination, [165] found at pages 403 and 404?

A. No, but I suggest that you introduce the record. I won't have any objection to your doing it. If you will do it for that purpose, it can be scanned over by us before argument.

Mr. Reilly: I do not like to introduce the whole record, unless it can be stipulated that it is introduced solely for the purposes of the present hearing. There are a great many statements in there.

(Testimony of Sidney Teiser.)

I do not know all of them, of course. I am not familiar with the case—some of them might be taken against us on the merits, and I do not know the case well enough to be willing to offer the whole record as part of my evidence.

Mr. Teiser: I think if you will look at that record you will find that the first statement about this case was not by me, because I am quite positive I knew nothing about this case until it was brought up by others.

Mr. Reilly: I will say to the court that I have not found that to be a fact. I might not have read it right, but the first reference to the cases being named that I find in there was by yourself, Mr. Teiser. I think that is all.

(Witness excused.)

The Court: There has been so much talk about this Bank of California credit file. Why isn't it in evidence?

Mr. Teiser: I will state to your Honor why. When the case of the Bank of California was concluded, a stipulation was entered into, and the Bank of California withdrew all the exhibits [166] that they introduced, by permission of the court. We did not withdraw any of ours, but the clerk called me up and insisted upon my taking away the records, in view of the fact that we had a stipulation drawn, and that they were cluttering up the office, and the case was closed, so I took the records. The Bank of California had its records and I had mine.



I tried to call Mr. Borden Wood this forenoon to see whether I could get that Bank of California credit file, but I could not get hold of Mr. Borden Wood. I have not had an opportunity to get him, but that is the situation. That particular credit file was withdrawn by the Bank of California.

Mr. Reilly: As far as we are concerned, we had never heard of the credit file until the present time.

The Court: Incidentally, I read it in connection with this other case. I read it very thoroughly and know pretty well what is in it.

Mr. Reilly: I would have liked at least to have been able to have seen it. I do not know what is in it or whether I would want to offer anything that is in it, but if your Honor would permit that matter to be looked into further, it may be that we would want to offer it.

Mr. Teiser: It would be very difficult, if your Honor please. I do not know how near we are to the end of this case.

Mr. Reilly: I would say we are almost through. I have one more witness. [167]

Mr. Teiser: I do not know how long your Honor expects to listen to argument, but if it is not going to be argued immediately, at least, the matter can be held over until I can see if I can get the credit file.

The Court: I think it might be advisable.

Mr. Teiser: If I can get it, of course, I will tender it in evidence.

Mr. Reilly: In the Bank of California matter, your Honor, I had marked as Pre-Trial Exhibits



various parts of that record which seemed to me to be pertinent, at the time of pre-trial. I think they include your Honor's opinion and other matters there. I see somebody has very carefully stapled them together. They are marked there as Pre-Trial Nos. 89 to 102, inclusive. I now offer those parts of the record in evidence.

Mr. Teiser: I object to the introduction, if your Honor please, first, because in regard to many of them they have no evidential value in this phase of the case; secondly, if the record is going to be introduced, I insist upon the whole record being introduced and not a part of it culled out from the whole.

Mr. Reilly: As far as the whole record is concerned, that may be a matter that the plaintiff may desire to do, but I do not think I should be limited; if I want to produce and introduce parts of the record considered pertinent, I do not think I should be called upon to introduce the whole, or vouch for [168] any part of it, other than those portions I have in mind.

The Court: If you wish to offer the rest of it, I will receive it.

Mr. Teiser: I do.

The Court: No question about the transcript? No question about the authentication of the transcript?

Mr. Reilly: Oh, no.

(Copy of amended petition in case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage

Company, previously marked and identified as defendant's Pre-Trial No. 89, thereupon received in evidence and marked Defendant's Exhibit No. 89.)

(Copy of findings of fact in case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial No. 90, thereupon received in evidence and marked Defendant's Exhibit No. 90.)

(Copy of motion of the Bank of California in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial No. 91, thereupon received in evidence and marked Defendant's Exhibit No. 91.) [169]

(Copy of affidavit of Harvey N. Black, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 92, thereupon received in evidence and marked Defendant's Exhibit No. 92.)

(Copy of affidavit of W. Lair Thompson, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 93,

thereupon received in evidence and marked Defendant's Exhibit No. 93.)

(Copy of opinion of Honorable James Alger Fee, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 94, thereupon received in evidence and marked Defendant's Exhibit No. 94.)

(Copy of order upon motion to rehear and rehearing, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 95, thereupon received [170] in evidence and marked Defendant's Exhibit No. 95.)

(Copy of testimony of E. E. Gallagher, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 96, thereupon received in evidence and marked Defendant's Exhibit No. 96.)

(Copy of testimony of R. Erickson, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 97, thereupon received in evidence and marked Defendant's Exhibit No. 97.)

(Copy of testimony of William Kennedy, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 98, thereupon received in evidence and marked Defendant's Exhibit No. 98.)

(Copy of testimony of Thomas G. Greene, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 99, thereupon received in [171] evidence and marked Defendant's Exhibit No. 99.)

(Copy of colloquy between counsel, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 100, thereupon received in evidence and marked Defendant's Exhibit No. 100.)

(Copy of testimony of E. F. Munly, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 101, thereupon received in evidence and marked Defendant's Exhibit No. 101.)

(Copy of testimony of George M. McBride, in the case of the Bank of California, N.A., versus George McBride, Trustee of Western

Bond and Mortgage Company, previously marked and identified as defendant's Pre-Trial 102, thereupon received in evidence and marked Defendant's Exhibit No. 102.)

The Court: What exhibit is that to which you referred, the Bank of California matter?

Mr. Reilly: 103 and 103-A. There are two volumes, Pre-Trial 103 and Pre-Trial 103-A, plaintiff's Pre-Trial Exhibit.

I want to make an objection. The defendant objects [172] to the reception of the whole of the testimony, the whole transcript, insofar as any part of it purports to be substantive evidence against the defendant.

The defendant has no objection to its being considered solely in connection with the question of the statute of limitation and laches.

The Court: The Court will admit it, subject to the objection.

(Transcript of record in the case of the Bank of California, N.A., versus George M. McBride, Trustee of Western Bond and Mortgage Company, a corporation, bankrupt, No. 10,062, consisting of two volumes, previously marked and identified as plaintiff's Pre-Trial Exhibits 103 and 103-A, thereupon received in evidence and marked Plaintiff's Exhibit No. 103 and No. 103-A, respectively.)

Mr. Reilly: The defendant now offers the answer of the Western Bond and Mortgage Company and the Beacon Investment Company in the case

of Brockie against the Western Bond and Mortgage Company, et al on defendant's Pre-Trial 66.

The Court: Just offer them all at once. Is there any objection to that?

Mr. Teiser: I have an objection to that, your Honor, in view of the fact that the complaint has been introduced and these other documents. I assume the objection will be overruled. [173]

The Court: Overruled.

(Answer of Western Bond and Mortgage Company and Beacon Investment Company in the case of John Brockie versus Western Bond and Mortgage Company, and others, previously marked and identified as defendant's Pre-Trial 66, thereupon received in evidence and marked Defendant's Exhibit No. 66.)

Mr. Reilly: The defendant offers defendant's Pre-Trial 67, being the answer of C. H. Farrington in that same case.

Mr. Teiser: The same objection.

The Court: The same ruling.

(Answer of C. H. Farrington in the case of John Brockie versus Western Bond and Mortgage Company, et al, previously marked and identified as defendant's Pre-Trial 67, thereupon received in evidence and marked Defendant's Exhibit No. 67.)

Mr. Reilly: We offer in evidence defendant's Pre-Trial No. 70, being the Court's journal record of the motion of the plaintiff to dismiss the complaint in that same case.



Mr. Teiser: The same objection to that.

The Court: Admitted.

(Journal entry of the District Court of the United States in the case of Brockie vs. Western Bond and Mortgage Company, et al, July 27, 1931, previously marked and identified as defendant's [174] Pre-Trial 70, thereupon received in evidence and marked Defendant's Exhibit No. 70.)

Mr. Reilly: We offer in evidence, if the Court please, defendant's Pre-Trial 69, consisting of a brief filed by the defendant, including the defendant Farrington, to the motion to dismiss.

Mr. Teiser: Object to that as a self-serving statement.

The Court: The objection is overruled.

(Copy of memorandum of defendants Laurel Investment Company, Western Guaranty Company and C. H. Farrington, opposing motion of plaintiff to dismiss in the above case, previously marked and identified as defendant's Pre-Trial 69, thereupon received in evidence and marked Defendant's Exhibit No. 69.)

Mr. Reilly: The defendant offers defendant's Pre-Trial 71, the order dismissing the suit.

Mr. Teiser: No objection.

The Court: Admitted.

(Copy of order dismissing suit in the case of John Brockie versus Western Bond and Mortgage Company, et al, previously marked

and identified as defendant's Pre-Trial 71, thereupon received in evidence and marked Defendant's Exhibit No. 71.)

Mr. Reilly: We offer the following newspaper articles: [175] defendant's Pre-Trial 72, copy of an article from the Oregon Journal of July 13, 1931; defendant's Pre-Trial 73, copy of an article from the Oregonian of July 14, 1931; defendant's Pre-Trial 75, copy of an article from the Oregon Journal of July 14, 1931; and defendant's Pre-Trial 76, copy of an article from the Oregonian of July 15, 1931. Those are all newspaper articles.

Mr. Teiser: Object to the introduction of them, first, because they have no materiality in the matter; not shown to have been brought to the attention of the Trustee, nor that he was chargeable with notice of them.

The Court: Objection overruled. They may be admitted.

(Copy of article from the Oregon Journal of July 13, 1931, previously marked and identified as defendant's Pre-Trial 72, thereupon received in evidence and marked Defendant's Pre-Trial Exhibit No. 72.)

(Copy of article from the Oregonian of July 14, 1931, previously marked and identified as defendant's Pre-Trial 73, thereupon received in evidence and marked Defendant's Exhibit No. 73.)

(Copy of article from the Oregon Journal of July 14, 1931, previously marked and identified

as defendant's Pre-Trial 75, thereupon received in evidence and marked Defendant's Exhibit No. 75.)

(Copy of article from the Oregonian of July 15, 1931, [176] previously marked and identified as defendant's Pre-Trial 76, thereupon received in evidence and marked Defendant's Exhibit No. 76.)

Mr. Reilly: The defendant offers in evidence defendant's Pre-Trial 77, consisting of a motion, with an affidavit, filed in the case of Edward Pape and others versus the Western Bond and Mortgage Company and others, in the Circuit Court of Oregon, for Multnomah County.

Mr. Teiser: May I ask the Court whether it is proposed to introduce the complaint in that case?

Mr. Reilly: I thought I had. I thought it was in the pre-trial exhibits, but I do not find it among my belongings. It is not among the pre-trial exhibits.

I offer this motion for the purpose of showing other suits pending, this motion being in the Pape case.

Mr. Teiser: I object to the introduction of this motion as a part of the record in the Pape case, unless the whole is introduced, and then I would object to the whole on the same ground that I objected to the other.

The Court: Is that a pre-trial exhibit?

Mr. Teiser: Yes, your Honor.

Mr. Reilly: Yes.

The Court: What is the number of it?

Mr. Reilly: No. 77.

The Court: I will amend the pre-trial order to make exhibit [177] 77 the whole file in that case.

Mr. Reilly: I haven't the whole file, your Honor. It would take some little time to make the whole file available. I offer this part of the file.

The Court: All right. Refused.

Mr. Reilly: The defendant offers defendant's Pre-Trial 82, consisting of an article from the Oregonian of August 4, 1934. It seems to be out of order.

Mr. Teiser: What date is that?

Mr. Reilly: August 4, 1934.

Mr. Teiser: What number?

Mr. Reilly: That is No. 82.

Mr. Teiser: Object to it for the same reason, your Honor.

The Court: Admitted.

(Copy of article from the Oregonian of August 4, 1934, previously marked and identified as defendant's Pre-Trial 82, thereupon received in evidence and marked Defendant's Exhibit No. 82.)

Mr. Reilly: We next offer defendant's Pre-Trial 84, being the copy of an article from the Oregonian of August 19, 1931.

Mr. Teiser: The same objection.

The Court: The same ruling.

(Copy of article from the Oregonian of August 19, 1931, previously marked and identified as defendant's Pre-Trial 84, thereupon re-

ceived in evidence and [178] marked Defendant's Exhibit No. 84.)

Mr. Reilly: Defendant's Pre-Trial 85 is the copy of an article from the Oregon Journal of September 10, 1931. We offer that in evidence.

Mr. Teiser: The same objection.

Mr. Reilly: In that connection, your Honor, I stated to your Honor this morning that these constitute all of the newspaper articles in 1931. On further reflection, I should say up until the last article in September. There may have been articles later, I don't know.

The Court: Admitted.

(Copy of article from the Oregon Journal of September 10, 1931, previously marked and identified as defendant's Pre-Trial 85, thereupon received in evidence and marked Defendant's Exhibit No. 85.)

Mr. Reilly: The defendant offers in evidence defendant's Pre-Trial 87, being a copy of an order for the examination of books in the case of Thompson versus Western Bond and Mortgage Company.

Mr. Teiser: I object to the materiality; object to the introduction of this pre-trial exhibit; object to the materiality of it. How could we be chargeable with an order permitting the examination of books by Mr. McCurtain in another case?

The Court: No. 86 is already in?

Mr. Reilly: 86 is in. [179]

The Court: No. 87 is admitted.

(Copy of order of October 6, 1931, in the

case of H. C. Thompson, et al, versus Western Bond and Mortgage Company, et al, in the Circuit Court of Oregon for Multnomah County, previously marked and identified as defendant's Pre-Trial 87, thereupon received in evidence and marked Defendant's Exhibit No. 87.)

Mr. Reilly: We offer defendant's Pre-Trial 88, being copy of an affidavit of Allen H. McCurtain in that same case.

Mr. Teiser: Objected to for the same reason.

The Court: Yes, the same objection; admitted.

(Copy of affidavit of Allen H. McCurtain in the case of H. C. Thompson, et al, versus Western Bond and Mortgage Company, et al, in the Circuit Court of Oregon for Multnomah County, heretofore marked and identified as defendant's Pre-Trial 88, thereupon received in evidence and marked Defendant's Exhibit No. 88.)

Mr. Reilly: We next offer defendant's Pre-Trial No. 106, being the copy of an order appointing or authorizing the employment of Messrs. Teiser and Keller, attorneys for the Trustee.

Mr. Teiser: I do not see what materiality that has.

The Court: Your petition is already in, the petition for appointment. [180]

Mr. Teiser: Did that go in? I thought I was just questioned about it. Immaterial. I make that objection.



The Court: That was No. 104. That was already admitted.

Mr. Teiser: I do not see the materiality. It certainly has no bearing in this case if we were employed as attorneys.

Mr. Reilly: Shows the date when your duties started.

The Court: Objection overruled. It will be admitted.

(Copy of order appointing counsel for Trustee in the matter of Western Bond and Mortgage Company, Bankrupt No. B-16772, previously marked and identified as defendant's Pre-Trial 106, thereupon received in evidence and marked Defendant's Exhibit No. 106.)

Mr. Reilly: We next offer in evidence defendant's Pre-Trial 109, being an order confirming agreement regarding attorneys' fees.

Mr. Teiser: Objected to for the same reason.

The Court: Overruled.

(Copy of order confirming agreement regarding attorneys' fees, previously marked and identified as defendant's Pre-Trial 109, thereupon received in evidence and marked Defendant's Exhibit No. 109.)

Mr. Reilly: We next offer defendant's Pre-Trial No. 110, being an order directing the Trustee to pay certain expenses.

The Court: What is that about? [181]

Mr. Reilly: I beg your pardon?

The Court: What is that about?

Mr. Reilly: The claim was made of lack of funds. This shows that they were in funds.

Mr. Teiser: Let me see that letter, please.

Mr. Reilly: Shows over a thousand dollars.

Mr. Treiser: If your Honor please, this payment of expenses was had in connection with the Besson and Brown case. After the Besson and Brown case was filed and after the compromise was made with Besson and Brown, it shows that some \$1655.65 was paid out for expenses, including attorney's fees, and I just do not see that that has any bearing in this case. The fact is there is no claim here that we did not have any funds until—I mean that we did not have any funds after we recovered in this case. Obviously, we did then have funds.

The Court: What is the date of that?

Mr. Reilly: May 27, 1938.

The Court: It will be admitted.

(Copy of order directing Trustee to pay certain expenses, previously marked and identified as defendant's Pre-Trial 110, thereupon received in evidence and marked Defendant's Exhibit No. 110.)

Mr. Reilly: The next one is defendant's Pre-Trial 111, financial report and statement of the Trustee. It was filed February 24, 1943, but covers the period from December up to [182] that time, showing the financial condition of the estate.

Mr. Teiser: It seems to me, your Honor, while it has no deleterious effect that I know of, it is just cluttering up the record.

The Court: No, I think I won't refuse it on that ground. I think it is material in this way, insofar as it shows that during that period the Trustee was under obligation to investigate, and if he had funds to do it, it may be relevant.

Mr. Teiser: It don't show that.

The Court: I do not know anything about that. There is no ground for its exclusion on the theory that it is immaterial. The objection is overruled.

(Copy of financial report and petition of Trustee, previously marked and identified as defendant's Pre-Trial 111, thereupon received in evidence and marked Defendant's Exhibit No. 111.)

Mr. Reilly: We next offer a letter marked defendant's Pre-Trial 112, being a copy of a letter from Mr. Erickson, accountant, proposing terms of employment, which were accepted.

Mr. Teiser: May I ask whether that is the letter that was handed to Mr. Erickson heretofore?

Mr. Reilly: Yes, and the Court refused to permit its introduction on cross-examination.

The Court: Admitted.

(Copy of letter dated July 20, 1936, from R. Erickson [183] to Sidney Teiser, previously marked and identified as defendant's Pre-Trial 112, thereupon received in evidence and marked Defendant's Exhibit No. 112.) [184]

## ROBERT T. JACOBS

was thereupon produced as a witness on behalf of the defendant and, being first duly sworn, was examined and testified as follows:

## Direct Examination

By Mr. Reilly:

Q. What is your occupation, Mr. Jacobs?

A. I am an attorney.

Q. You have been a resident of Portland how long?

A. About twenty-five year.

Q. In connection with what has been called here the Western Guaranty transaction, do you know who handled the legal phase of that for Mr. Farrington?

A. Yes, Mr. Arthur C. Spencer handled it.

Mr. Teiser: I object to the question and answer and ask that the answer be stricken. I don't know the purpose of it. I cannot see the materiality of it.

The Court: I do not see it right now.

Mr. Reilly: The purpose *if*, your Honor, is this: there are two defenses, the statute of limitations and laches, and we are offering this to show that a witness who was familiar with the transaction, an important witness, is now dead.

The Court: Go ahead.

Q. Did you, on behalf of Mr. Farrington, have occasion to consult with Arthur Spencer concerning this transaction?

A. I did. [185]

Q. More than once?

(Testimony of Robert T. Jacobs.)

A. Yes, as I recall some two or three times during the working out of the agreement between Mr. Farrington and the purchasers of his interest.

Q. Who handled the matter on the other side, on the Massachusetts Mortgage Company side?

A. The seller and buyer were brought together by a man by the name of Edmunds, and Mr. O'Flynn represented the purchaser.

Q. I have forgotten whether there is any testimony as to Mr. O'Flynn or not. Is Mr. O'Flynn still living?

A. No, he is not.

Q. I will ask you whether or not he died more than two years ago.

A. Yes. I am informed he died prior to 1942. That is the information that I have.

Mr. Teiser: I object to that testimony as hearsay. I am willing to stipulate——

Mr. Reilly: Do you question his death?

Mr. Teiser: No. I am willing to stipulate that Mr. O'Flynn died during the pendency of the Western Bond and Mortgage Company suits, I mean, during the pendency of the Bank of California suit, originally tried before appeal.

Q. When did that terminate?

A. As I recall, that terminated—I think Mr. O'Flynn died at least five years ago, at least five years ago. [186]

Mr. Reilly: That is sufficient for our purposes. That is all.

(Testimony of Robert T. Jacobs.)

Cross-Examination

By Mr. Teiser:

Q. Mr. Jacobs, you say you know Mr. Spencer was handling this matter on behalf of whom?

A. Of Mr. Farrington.

Q. On behalf of Mr. Farrington?

A. That is right.

Q. In what year?

A. 1930, December, 1930. Let's see, either 1929 or 1930, either December, 1929 or 1930, I do not recall which, but it was one of the two.

Mr. Teiser: That is all.

Mr. Reilly: That is all.

(Witness excused.)

Mr. Reilly: Now, with the exception of that Bank record, that is our case, your Honor.

The Court: Anything further?

Mr. Teiser: We have nothing to offer.

Mr. Reilly: In the argument of this case, I believe it ought to be submitted on briefs. It is too important a matter, there is too much involved, to be handled on oral argument.

Mr. Teiser: I agree with that. If your Honor agrees, both [187] sides will submit briefs. In fact, I have a brief of the law on the question of the statute of limitations. It is written merely for the purpose of briefing the law on that, but I take it your Honor would also want arguments as well as briefs.

Mr. Reilly: I have no objection to oral argument



following the filing of the briefs. We ought to have briefs on the law before the Court in any event.

The Court: My attitude is this: you go ahead and file your briefs and if I feel I want to have oral argument after I read the briefs, I will call on you for it.

Mr. Reilly: Very well, your Honor. What are we going to do about admitting this bank record?

Mr. Teiser: What?

Mr. Reilly: Admitting the files in connection with the bank record.

Mr. Teiser: As soon as I get around to the office, I will call up Mr. Wood, because my understanding was with him that if we needed any of these records they would be available.

Mr. Reilly: What do you say we go to see him together?

Mr. Teiser: Why certainly, I have no objection to that. Certainly. You are welcome to go with me. We will get that record as soon as we can from the Bank of California.

Mr. Reilly: I am wondering if we should set a time now or shall we advise your Honor when we have the evidence?

The Court: I would like to see the file before it is marked [188] as a pre-trial exhibit.

Mr. Teiser: Suppose I notify your Honor within the week as to whether or not the record is available and, if available, we can come up here and offer it in evidence.

Mr. Reilly: And your Honor could then fix a date so we could wind this up.

The Court: Yes. As a matter of fact, I can fix a date now, assuming that you will find it before the end of the week. I can fix a date——

Mr. Reilly: Fix what, your Honor?

The Court: I can fix a date for you to submit briefs now. You don't need to worry about that.

Mr. Reilly: I was thinking more of the time for getting these documents.

Mr. Teiser: I am just wondering, if we are going to write briefs and they are going to have the thoroughness that your Honor would expect, and would have the right to expect, if it would not be better to have the testimony transcribed so that we may be able the better to refer to the testimony and the exhibits. I take it it would be a more intelligent brief, written with the record before us.

(Colloquy between Court and counsel.)

The Court: I assume probably the only thing we can do is to have the testimony transcribed. Somebody may want to appeal. Anyway, we might as well get it in written form so that we can [189] see what was said.

Mr. Teiser: Suppose I suggest that ten days after the transcription is delivered to us the plaintiff's brief be filed and that the defendant have ten days to file his brief, and then let us have a reasonable time to file our reply brief.

The Court: All right, ten, ten and five, after the transcript is in your hands.

(Thereupon the proceedings had in the above entitled cause on to-wit: November 29, 1944, were concluded.) [190]

Wednesday, December 6, 1944

2:00 o'clock P.M.

Court reconvened pursuant to adjournment.

Mr. Reilly: Shall we proceed, your Honor?

The Court: Yes.

Mr. Teiser: If your Honor please, I told your Honor I would have the exhibits which I referred to in my testimony before the Court.

I contacted Mr. Wood and had him obtain from the Bank of California that exhibit. It is here. An order for a subpoena duces tecum was entered, and Mr. Wood is here with the exhibit for the purpose of presenting it to the Court and for the purpose of introducing it as an exhibit in the case.

The Court: You want to put him on the stand?

Mr. Teiser: Yes.

Mr. Reilly: Are you going to examine him, or may I?

Mr. Teiser: I just want to have him identify this.

Mr. Reilly: You may examine him, if you want. I subpoenaed him, but you may examine him if you want to.

Mr. Teiser: I think you did it at my request.

Mr. Reilly: All right. Go ahead. [191]

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## BORDEN WOOD

was thereupon produced as a witness on behalf of the plaintiff and, being first duly sworn, was examined and testified as follows:

(Testimony of Borden Wood.)

Direct Examination

By Mr. Teiser:

Q. Mr. Wood, did you bring with you the exhibit which was introduced by McBride, Trustee, in the matter of the show cause against the Bank of California, entered in the case of the Western Bond and Mortgage Company, Bankrupt?

A. I have, Mr. Teiser. I brought that.

Q. Was it marked or has it been marked with an exhibit mark?

A. It is marked "Trustee's Exhibit 31."

Q. Sir?

A. It is marked "Trustee's Exhibit 31."

Mr. Teiser: If your Honor please, I offer that in evidence.

Mr. Reilly: There is only one question, your Honor, and that is all of these newspaper articles—I have checked them against those that are in evidence. I think all of the newspaper articles from the Oregonian and Journal that are in evidence—that are in there have already been introduced by me, but I find them different in this particular, that the young lady who copied them did not copy the headlines. I do not know whether your Honor wants us to introduce the file. Mr. Wood said the Bank would like to have the file back.

I have no objection, except I thought that I would [192] tell your Honor we are duplicating these exhibits. I have checked them over, and they are exhibits 63, 65, 73, 76, 78, 80, 83 and 84.

(Testimony of Borden Wood.)

Mr. Teiser: Do I understand what you want to do, or what you are willing to do is to stipulate that the file which has been referred to and which Mr. Wood has here, contains articles which you have introduced in evidence in the trial?

Mr. Reilly: It contains some other things.

Mr. Teiser: Yes.

Mr. Reilly: I do not know how important it is to the Bank to have the file back immediately. I have no objection to the whole file going in, but I ought to explain to your Honor that in some instances there is a duplication.

Mr. Teiser: I am perfectly willing to stipulate with you that this file contains the articles that you have stated, if you have checked them.

Mr. Reilly: I have checked them as well as one person can check.

Mr. Teiser: I am perfectly willing to stipulate that the file which is here, and which is referred to in my testimony, contains the articles that were introduced in evidence by the defendant in this matter. It contains other things and other articles, but it at least contains those.

The Court: Yes.

Mr. Reilly: Yes, and contains the exhibits whose numbers I [193] have indicated. There is that difference between the copies that I have put in and the actual articles, and that is the headlines, and they vary in size. It might be better that this file be in rather than the typewritten copies which do not contain the headlines.

(Testimony of Borden Wood.)

Then, there are some other articles there. I do not know just how important they are—some letters.

That file itself was in the possession of Mr. Teiser at the original trial in the Bank of California case, and also in his possession at the time he examined Mr. Brown and Dr. Besson.

Mr. Teiser: I beg to differ with you. The file was never in my possession. We brought it to the court, the Bankruptcy Court, or the Bank of California did upon our request, when they said they had it, and it was immediately introduced in evidence from the Bank's possession. We never had it in our possession.

Mr. Reilly: There are one or two questions I want to ask Mr. Teiser about the file. Does your Honor desire us to keep the whole file or let the old copies stand?

The Court: You are trying the lawsuit. I am just the Judge. You may introduce it or not, just as you please. I have no interest in that.

Mr. Teiser: I am perfectly willing to stipulate——

Mr. Reilly: I will say this: I think now I am going to [194] offer it in evidence and will ask later, if the Bank desires, for permission to substitute copies of the whole file.

The Court: I am only going to rule on one thing. Mr. Teiser has offered it in evidence. Do you object?

Mr. Reilly: I do not object, no.



(Testimony of Borden Wood.)

The Court: All right. Admitted. I will assure Mr. Wood that whatever the Bank wants to do, we will see that arrangements are made for you to get it.

Mr. Teiser: There is no reason for Mr. Wood waiting?

The Court: Excused.

The Witness: Thank you.

(Witness excused.)

Mr. Teiser: May the exhibits be marked with the next number?

Mr. Reilly: It is not in the pre-trial proceedings.

The Court: I want the pre-trial order.

Mr. Reilly: I think I have a copy of the pre-trial order.

The Court: I want the amended pre-trial order. I will wait and get it. I am sending out for it.

Mr. Reilly: Shall we proceed with questions we want to ask Mr. Teiser?

The Court: Yes, if you wish.

Mr. Reilly: I do not see any particular reason for him coming up on the stand.

The Court: I do. If he is going to testify in the case, he is going to take the witness stand. [195]

Mr. Teiser: No objection, your Honor, at all.

## SIDNEY TEISER,

having previously been duly sworn, was recalled as a witness on behalf of the defendant and was examined and testified as follows:

## Direct Examination

By Mr. Reilly:

Q. The exhibit which has just been received, which was previously marked Trustee's Exhibit 31, which consists of the credit file of the Bank of California relating to the Western Bond and Mortgage Company, that was introduced by you in evidence in the hearing on the show cause order in November, 1936, subsequent to the time you had cross-examined Mr. Greene about the Brockie, Thompson and Pape cases, was it not?

A. I just could not say. It would be impossible for me to remember now. I want to be careful, so I could not say what the order of introduction of the testimony some nine years ago was—eight years ago—but the record is in. The record or the transcript of record that went to the Circuit Court of Appeals, that certainly would show the order in which it was introduced.

Q. You had that credit file in your hands at the time you examined Dr. Besson and Mr. Brown in February, 1937, did you?

A. I don't know. I don't know. What happened was that during the course of the testimony, I think Mr. Greenwood—it was [196] brought out from Mr. Greenwood, who was Manager of the

(Testimony of Sidney Teiser.)

Bank of California or an officer of the Bank, that there might be a credit file. During the recess or while the Court was waiting, he sent for the file and got it and brought it up to the court. It was then introduced by me from his hands in the case.

Q. I am not talking about that.

A. Now, wait a minute. It became an exhibit in the case. I did not, as far as I know, withdraw any exhibits in that case for the purpose of examining Besson and Brown, but I did refer or had reference to the articles that I had seen in that file, because those were the only newspaper articles in 1931 that I saw or had in mind in 1936, or the time of the Besson and Brown trial.

Q. Did you not have in your hands the newspaper articles that you showed to both Dr. Besson and Mr. Brown?

A. I might have, and if I did it was in that file, but I did not withdraw the file from the files of the case.

Q. Did you have any other newspaper articles except those that were in the file?

A. I am quite positive I did not. That is why I testified the newspaper articles that I referred to were in that file. I know I did not make any search of newspaper records for the year 1931 or any time previous.

The Court: The Court at this time amends the pre-trial order, by consent, by adding to plaintiff's exhibits, plaintiff's [197] Exhibit No. 162, the credit file of the Bank of California which has just been introduced.

(Testimony of Sidney Teiser.)

Mr. Reilly: 162, the credit file of the Bank of California?

The Court: Yes, No. 162.

(Credit file of Bank of California, in re Western Bond and Mortgage Company, there-upon received in evidence and marked Plaintiff's Exhibit No. 162.)

Mr. Reilly: 162, credit file, Bank of California.

The Court: Yes.

Mr. Reilly: N. A.?

The Court: I did not put it on.

Mr. Reilly: That is all right. I just want to get an exact copy.

Q. In examining Mr. Brown, you said "I show you some articles taken from the Oregonian." You remember you did so? A. Yes.

Q. Does that refresh your memory as to whether this file, plaintiff's Exhibit 162, was in your hands?

A. No, it don't refresh my memory, except I would say that I showed him the articles and the only articles that I had were in that file and, as a logical consequence, it would have to be that I had the file, but I have no recollection about it at this time as to whether the file was in my hands or not.

Q. You did not take the file apart? [198]

A. Oh no.

Q. Would you say that it contained not only newspaper articles of 1931 but also those of 1934, at all times that you had anything to do with it?

A. I would answer that by saying I did not take the file apart. If I had the file in my hands,

(Testimony of Sidney Teiser.)

it was the whole file. I undoubtedly was referring to the articles, as the context of the examination showed, referring to articles which showed the insolvency of the Western Bond and Mortgage Company. That was the only purpose that could have been asked of Besson and Brown, the only reason for asking Besson and Brown about that. It was necessary to show that they had knowledge of that at the time, whether or not the Western Bond and Mortgage Company was bankrupt or insolvent.

Q. Are you prepared to admit you did read all of the newspaper articles contained in that credit file?      A. Read it?

Q. Not later than February, 1937?

A. I am prepared to admit that I read it?

Q. Are you prepared to admit that you read those articles?

A. I am prepared to deny that I read them.

Q. You are prepared to deny that you read the articles?      A. Absolutely.

Q. Are you prepared to deny you read any of the articles?

A. I know that I read or knew the contents of articles in that [199] file that had reference to the insolvency or bankruptcy of the Western Bond and Mortgage Company.

Q. All right. Show me the articles in 1931 in the file that you admit having read.

A. Well——

Q. Prior to taking the Brown and Besson depositions.

(Testimony of Sidney Teiser.)

A. You want an admission now as counsel, or my recollection as to——

Q. I am asking you as a witness.

A. What?

Q. What are the articles in the file in the credit file, plaintiff's exhibit 162, that you now admit you read prior to taking Besson's and Brown's testimony?

A. All I can say——

Mr. Reilly: I want the file. Will you please hand the credit file to the witness? May we have it, your Honor?

The Court: Yes.

A. Incidentally, may I call attention to the fact that there are some papers in this file that are now in here that were not in there at the time of the 1936 proceedings?

Q. I imagine there are some letters in there, possibly. There are loose articles in there; I think one from the Oregonian, telling about the bringing of this case.

A. I think, as a matter of fact, everything that was in the file at the time is shown by the mark of the Clerk on each page.

Q. I see. All right. [200]

A. From an examination of these newspaper articles, I would have to say, strange as it may seem, that either some of the newspaper articles have been removed from the file, which I doubt, or we did not have this file, because I know, subject to such mistakes that a human mind would make, I know the articles that I handed to Besson and



(Testimony of Sidney Teiser.)

Brown were articles which were concerned with the bankruptcy or insolvency of the Western Bond and Mortgage Company.

Q. In the early part of 1931?

A. I don't know about the early part.

Q. That is what you said in your testimony.

A. I don't know. Whenever they were filed—whenever the articles were issued. The only purpose I could have had, under any circumstances, in the Besson and Brown suit for showing them any newspaper articles, was to show that they knew that the Western Bond and Mortgage Company was insolvent. What other purpose could I possibly have had?

Q. I want to ask you what newspaper articles you showed them.

A. Sir?

Q. You have given one explanation, that the newspaper articles were in the Bank of California credit file?

A. I certainly did.

Q. Do you deny that?

A. Deny it?

Q. Yes. [201]

A. I will say this, in looking over the file here the few minutes that I have looked it over—and I think I have looked it over with reasonable thoroughness—that I do not see any articles in here concerning the filing of a petition against the Western Bond and Mortgage Company, any article in 1931. The other articles that refer to the filing of the petition evidently were in 1934, but the articles, the newspaper articles that are attached to this file which bear inserted dates, either pen or typewriter,

(Testimony of Sidney Teiser.)

for the year 1931, do not seem to be articles referring to the bankruptcy.

Q. There was no bankruptcy started until November, 1931, you know that?

A. Yes, I think that is right.

Q. Now, will you answer my question? Do you deny having shown the articles in that credit file, written in the Oregonian or Journal early in 1931, to either Besson or Brown?

A. So far as reasoning back at this time is concerned, I would say that I did not show these articles in the file, dated 7/14—dated 1931, if I have read that right, to Besson and Brown.

Q. You saw these articles how long ago?

A. What articles?

Q. You saw this credit file with these articles in it, how long ago, recently?

A. Oh, I saw them when I went up to Mr. Wood's office to get Mr. Wood to obtain them from the bank.

Q. When was that?

A. And after he obtained the file from the bank, I went up there.

Q. Saturday morning?

A. Wait a minute. Yes, I think it was Saturday morning of last week.

Q. Having seen these articles, did you look for some other articles in the papers that you might have shown them?      A. At that time?

Q. Since Saturday morning?

A. No, sir. [203]

(Testimony of Sidney Teiser.)

Q. You made no attempt to find some other articles that you might have shown to Besson and Brown?

A. When I went up to look at this file?

Q. Answer that question, please.

A. No. You mean, since Saturday did I look for any newspaper articles since Saturday?

Q. Yes.           A. No, I have not.

Q. Did you say you have never seen this file with its present contents, those newspaper articles that are in there?

A. Certainly I have seen it. I have never said I did not see this file. I introduced it in evidence. I had it in my hands. I saw the file, I think, in the preparation of this brief before the Circuit Court of Appeals. I went through the exhibits in all probability and saw the file at that time, but I was not interested in that part of the file at all, in the case on appeal to the Circuit Court of Appeals. I was interested largely in the letter which the bank had in this file that I was supposed to have had in here. I don't know whether that is in here now.

Q. You say you did not examine these newspaper articles that were in that file, back during the trial in 1936?

A. I certainly do not recall examining them in 1936, not the newspaper articles that—not all the newspaper articles that are in this file. I don't recall—— [204]

Mr. Reilly: Would you pass to the witness the

(Testimony of Sidney Teiser.)

first volume of the transcript of testimony, exhibit 103? Would you please show him that?

Q. I will ask you to turn to page 414, to the statement made by you at that time, this being back in November, 1936: "I want to see these newspaper clippings referring to these various suits."

Does that refresh your memory as to whether you looked at them?

A. I don't see that, Mr. Reilly. What page is it?

Q. About the third place your name appears on page 414.

A. What is it?

Q. Where you said "I want to see these newspaper clippings referring to these various suits." Does that refresh your memory as to whether you examined these newspaper clippings?

A. No. I would say that I said "I want to see these newspaper clippings referring to these various suits," and with that in mind I objected to the bank withdrawing the file, to not introducing the file.

Q. You still say, after having read that, that you did not examine these newspaper clippings?

A. Mr. Reilly, all I can say is this: I have no recollection of reading the newspaper clippings, or these newspaper clippings. I have no recollection of reading them. That is all I can say. I may have read them. I certainly have no recollection [205] of reading them.

Q. May I ask whether it was following your reading of these newspaper clippings that you made the contract with the Trustee for a contingent fee

(Testimony of Sidney Teiser.)

to recover certain matters and transactions that you had discovered in the estate?

A. The contract or the order that was made in the case is certainly dated.

Q. The order is dated the 10th day of May, 1937?      A. May, 1937?

Q. Yes. The petition was filed in April, 1937. So, it was not until you had read these newspaper articles that you made this contract with the Trustee?

A. Wait a minute, Mr. Reilly. That cannot be so. I mean the fact cannot be so. I am not talking about the date of the order or even the petition, I don't think. I am sure of this, that Mr. McBride came up to the office——

Q. Are you answering my question or are you going off on something else?

A. I am trying to answer the best I can. I am trying to answer it and be honest.

Q. Go ahead.

A. Mr. McBride came up to our office and asked us whether we would handle for him, as Trustee, certain matters in connection with the Western Bond and Mortgage Company.

Q. That was June, 1936?      A. Sir? [206]

Q. That was in June, 1936, that order appointing you as attorney?      A. Correct.

Q. June, 1936?

A. The order for a contingent fee was almost a year later. In 1936, when the Trustee employed us, we had an understanding with him that we

(Testimony of Sidney Teiser.)

would handle the case, if it met with the approval of the Court, on a basis of a certain amount of recovery, and we suggested to him that, in order that there be no difficulty in this matter or no trouble in the matter, we would prefer to have the matter taken up with the creditors, in view of the fact that there were a thousand or more creditors, and any agreement we made was confirmed by the creditors and authorized by the Court before we undertook the litigation.

Q. What delayed you from June, 1936, until April, 1937, before you first filed your petition for the allowance of your one-third attorney's fees?

A. I don't know—just don't know, Mr. Reilly. It would seem to be the part of wisdom that we should have gotten that petition earlier, but if you say the petition was in 1937, if the date is there, I will take your word for it.

Q. There are some exhibits. You do not need to take my word. There is one other question I want to ask you.

Do you claim that you examined Dr. Besson and Mr. Brown [207] about the contents of newspaper articles, without your having read the newspaper articles?

A. Oh, I don't think that would be true.

Mr. Reilly: That is all.

(Witness excused.)

The Court: Is that all?

Mr. Reilly: That is all, your Honor.

The Court: Have you anything further?



Mr. Teiser: No, sir.

The Court: The cause is now submitted, I take it.

Mr. Reilly: It is, your Honor. We were to brief it, as I recall.

The Court: Yes.

Mr. Reilly: I do not know whether your Honor will permit me or not, but there was a question that I had in mind. It can be asked in the brief, just as well.

The statement was made by Mr. Teiser that he had learned the names of the three lawsuits pending in 1931 from Mr. Thompson's questions earlier in the case on the show cause order back in 1936, I having pointed out to him the place in the testimony where he had used the names and so forth in reference to the three suits.

I have examined the transcript of the testimony rather carefully, and I will ask counsel whether he will refer us to the page in the record where Mr. Thompson referred to these [208] cases by name or by attorneys. Is that a proper question to ask? Maybe he is not prepared to answer.

Mr. Teiser: I am not prepared to answer it, I don't think, Mr. Reilly. I don't think he referred to them by name at that time, before I used the names of Brockie or Pape, whichever one it was. I don't think in that testimony he referred to it. I may recall to you the fact that he examined Mr. Greene and others under 21-A, and that we got into a great deal of discussion in the hallway and other places. It might have been in some other way or in

some other manner that I got the word "Brockie." I don't know. I just don't know.

Mr. Reilly: Not only did you get the word "Brockie" but you also got the fact that Mr. McCurtain had a suit.

Mr. Teiser: Certainly. I testified to that. I testified that I talked to Mr. McCurtain.

Mr. Reilly: And also Little?

Mr. Teiser: I think I talked to Little or Little talked to me.

Mr. Reilly: That is all, now, your Honor.

The Court: Counsel was not under oath in this testimony. He is just making that statement as an attorney?

Mr. Reilly: I beg your pardon?

The Court: He is just making that statement as an attorney?

Mr. Reilly: I assume it would be just as binding on a client. [209]

The Court: I am just calling attention to the fact that when he is not on the witness stand he is not under oath.

Mr. Reilly: I do not want to put him back on the stand all the time. I will waive that part of it.

The Court: The Court now stands adjourned.

(Thereupon the proceedings had in the above entitled cause on, to wit, December 6, 1944, were concluded.) [210]

[Title of District Court and Cause.]

CERTIFICATE

I, Ira G. Holcomb, hereby certify that on, to wit, November 28-29, 1944, and December 6, 1944, I reported in shorthand certain testimony and proceedings had in the above entitled cause and court; that I thereafter caused said shorthand notes to be reduced to typewriting; and that the foregoing transcript, consisting of pages numbered 1 to 210, both inclusive, constitutes a true, full and accurate transcription of said shorthand notes, so taken by me as aforesaid, and of the whole thereof.

Dated at Portland, Oregon, this 8th day of December, 1944.

/s/ IRA G. HOLCOMB.

[Endorsed]: Filed Dec. 12, 1944. [211]

[Title of District Court and Cause.]

TRANSCRIPT OF PROCEEDINGS OF

MARCH 30, 1945

Portland, Oregon,  
Friday, March 30, 1945,  
11:35 A.M.

Before: Honorable James Alger Fee, Judge.

Appearances: Mr. Sidney Teiser, attorney for  
plaintiff; Messrs. John F. Reilly and Stephen  
Parker, attorneys for defendant.

Court Reporter: Cloyd D. Rauch.

PROCEEDINGS

The Court: I have gone through this case very carefully and have done a lot of work on it. After I got through I find that it is very nebulous as to what plaintiff's theory of the case is. I have gone through the briefs. Plaintiff has suggested [1\*] two different theories of recovery and the defense has suggested one. Neither of them clicks with the other. The briefs don't even meet. And I went carefully through the pre-trial order and I didn't find any solution of my difficulty there. Now, that has something to do with the statute of limitations, as you all know from briefing this trial, and I want to know that definitely before I say what I think. I called you in to find out what it is all about. In other words, I don't want to take a chance of deciding the case and deciding it on a

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\*Page numbering appearing at top of page of original Reporter's Transcript.

point that is not raised, apparently, in the case. If I go through this thing and then decide it, afterwards somebody might say that I decided it on a theory that nobody had done any talking about, so I want to know what we are talking about. So I think you had better explain, Mr. Teiser, what your idea and theory of the case is.

Mr. Teiser: Well, if your Honor please, it is a little difficult at this moment to get my thoughts back on the situation so hurriedly. I tried to read these briefs over this morning and I hadn't concluded doing so. Your Honor, if I understand you, wants to know on what theory the plaintiff brings this suit?

The Court: Well, now, I can help you out a little. The defendant, in his brief here, suggests that the theory of the case is different from the one that might be drawn from your original brief, and indicates that the defendant was of the [2] opinion that your case was initiated under 67, and you repudiate that in your reply brief and say that you are under Section 70, but not under 70 (e), but, instead, under 70 (a). Now, I want to know what distinction you think you draw between 70 (e) and 70 (a).

Mr. Teiser: Well, I can tell your Honor that right quickly, I think. I endeavored to state that in the reply brief, but 70 (a), as quoted on page 3 of the brief, provides that the trustee of an estate of a bankrupt "shall be vested by operation of law with the title of the bankrupt to all" and then "(4) property transferred by him in defraud of

his creditors;" and "(6) rights of actions arising upon contracts or from the unlawful taking or detention of, or injury to his property"; and, therefore, we are claiming, at least I think I could say among other things that we are claiming—that we are claiming the right by the trustee to title—or the title by the trustee in the property transferred by the bankrupt in fraud of his creditors and title to any action which the bankrupt may have from the taking of its property or injury to its property.

Now, under Section 70 (e) of the Bankruptcy Act—I should say 70 (a)—70 (e) of the Bankruptcy Act,—I haven't the language here, but—

The Court: Will you bring in the sections, both the originals and the new sections.

Mr. Teiser: —but I may say that, quoting from the summary [3] of Section 70 (e) contained in Davis against Wiley, and quoting from the language of the Court,—which the Court says is 70 (e)—but, under Section 70 (e), heretofore quoted, "The trustee may void any transfer which any creditor might have voided." The right is conferred upon the trustee to put him in position to assert the right which a creditor might have and recover, and the trustee is subrogated, and, therefore, under Section 70 (e) of the Act itself it seems to me, as I recall it, 70 (e) gives the trustee a right which he derives from creditors, a right which only the creditor would have—which he would have solely because the creditor had a right. In other words, a trustee acquires two rights, two kinds of rights, under the Bankruptcy Act,—maybe more,



but certainly two. One he acquires through the bankrupt himself by virtue of a title given to him under Section 70 (a); the other he acquires because he stands in the position of a creditor and by virtue of his assuming the position of creditor he acquires certain rights under 70 (e).

The Court: Well, you mean that the bankrupt could have set aside this transfer?

Mr. Teiser: The bankrupt could? Yes, sir.

The Court: You think the bankrupt could set aside——

Mr. Teiser: The Western Bond & Mortgage Company?

The Court: Yes.

Mr. Teiser: Why, certainly I think so. The bankrupt as against its officer, who—if our other portion of our claim is [4] right, we claim that the bankrupt and President of this corporation, in fraud of the corporation, himself transferred or caused to be transferred to himself, by manipulating his voting power, and so forth, certain assets, did it in fraud of the corporation. Now, if there were any corporation stockholders left, or directors left, not only could they have recovered it, but it would have been their duty to recover it, from the President, the property taken by him from the corporation. I can see no reason why the bankrupt could not have recovered, either before—of course, not after bankruptcy, because he would have the title there, but certainly it seems to me that the corporation itself could have recovered this property which was taken from it by the trustee.

Let's take the second cause of action, or we will call it the second claim. There we say that Mr. Farrington caused to be turned over to somebody some forty thousand, I think, shares of stock without getting any payment to the corporation therefor. I can't see why the corporation, if it discovered that situation, when it discovered that situation could not have brought suit, if there was anybody to bring it, to recover.

70 (e) of the Act—I will read it to your Honor. It says, "The trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided, and may recover," and so forth. In other words, under [5] 70 (e) it is an action which is subrogated—in which the trustee is subrogated thereto by creditors of the bankrupt, rather. But here we not only get the right of the bankrupt under 70 (a) by virtue of acquiring title himself, but also we get a title to set aside fraudulent transactions, under either theory, and that is why I say we do not have to confine ourselves to one title,—maybe we have to confine ourselves to one theory—but under 70 (a) the trustee becomes vested with property transferred by the bankrupt in fraud of his creditors, and also becomes vested with the title for the unlawful taking or detention of property or injury to his property.

The Court: Well, of course, I understand that you have the title of the bankrupt property transferred in defraud of creditors, but you are not suing for property transferred in fraud of creditors.

Mr. Teiser: No; I am suing to recover property transferred in fraud of stockholders, creditors,—I think I am. I think I am doing that, also. We are not suing in the name——

The Court: Just a moment. You aren't suing for property at all, as I understand your theory.

Mr. Teiser: We are suing for recovery of——

The Court: You are suing for recovery of damages for wrongful transfer.

Mr. Teiser: That is right.

The Court: That is an entirely different thing.<sup>4</sup> You don't [6] see that right as meaning that they are still the same thing, because they are not the same thing.

Mr. Teiser: No, we are not. We are not suing—your Honor is right about that—we are not suing to recover the thing itself. We are suing to recover damages for the transfer of the thing itself.

The Court—All right, where was the right of recovery of damages initiated?

Mr. Teiser: I didn't hear your Honor.

The Court: I say, where was the right of damages initiated in the first instance, in what person or rem?

Mr. Teiser: Well, prior to the election of the trustee, prior to the bankruptcy, the right to recover was in the bankrupt, in the corporation. After the election of a trustee it became vested in the trustee, as I see it.

The Court: Well, I think that is pretty definite, but that isn't made clear to me by your briefs, because your briefs are talking about Section 70

(a) and Section 70 (e) as though there was a distinction. Now, as I understand, there isn't any distinction on the suit that you are actually bringing. You are bringing, as I understand your present statement, action for recovery of damages for the wrongful transfer of property which initiated in the bankrupt and by virtue of the bankruptcy was transferred to the trustee.

Mr. Teiser: Yes, I think that is true, if I understand your [7] Honor's construction of my remarks, it is true that the action, cause of action, arose first in the corporation at the time of the taking, of the alleged taking.

The Court: Well, taking the matter now, it could not have arisen anywhere else.

Mr. Teiser: Why, I think not. I think not.

The Court: In other words, you do have a choice. You have a choice of saying it is a right that could have been enforced by the creditors and arose in them, or it is a right that arose in the bankrupt and the bankrupt——

Mr. Teiser: Well, I don't go that far. I don't want to quibble with your Honor, but I want to be clear.

The Court: No, I want to understand you, that is what I am trying to do.

Mr. Teiser: I am trying to be clear and to be frank. I think the cause of action first arose in the corporation—that is, a cause of action arose and became vested in the corporation at the time of the taking. Now, that doesn't mean also that creditors of the corporation wouldn't have a right to enforce

that cause of action. In other words, some creditor could have come in at that time if the bankrupt hadn't and enforced that right. Of course, I think your Honor will agree with that.

The Court: I understand that, but that is a derivative right.

Mr. Teiser: That is a derivative right that I think the creditor gets by virtue of the fact that the corporation had it, [8] and I think your Honor is right about that, although it is a little difficult to talk about derivative rights of creditors rather than stockholders. Undoubtedly this is true: If the bankrupt didn't have the right, certainly the creditor would not, under those circumstances, and it is because the bankrupt had the right and didn't assert it that the creditors can come in and assert it.

The Court: Well, we are clear, then, on this proposition, that it was a right which initiated in the bankrupt and was transferred to the trustee by virtue of the bankruptcy.

Mr. Teiser: Now, your Honor again uses a word, I think, a little loosely,—that is “transferred”—perhaps rightly uses that word by virtue of the law, of the Bankruptcy Act. It is an absolute transfer, as I indicated in my brief, not the same kind of transfer that comes from a receivership, for example, but the title itself goes to the bankrupt.

The Court: That is true. That is true, and some of the decisions characterize it as an inherited right.

Mr. Teiser: That is right.



The Court: We are correct about the nature of it.

Mr. Teiser: The nature of it, as I take it, comes because—I can't change that position—comes because, to use names, Farrington acquired or took property belonging to the bankrupt corporation, which the bankrupt corporation had a right to recover. Now, it went to persons, we will say, who it would not be proper [9] to recover it from, or it wasn't their choice to recover it from, so the trustee says, "I, having a right for the bankrupt to recover this property," now proceeds to recover. So undoubtedly it is because of the wrong done to the bankrupt, to the bankrupt first.

Now, we think, also, under that Section 70 (a) he also has a right—also has a right to recover, because he has title to property fraudulently transferred, and having title to property fraudulently transferred he may bring suit to recover that property or the value of that property.

Now, I think he had either or both of those rights, but we are not bringing suit on behalf of creditors; that is, we are not deriving, we are not claiming any derivative right, because of creditors, or, for that matter, because of the stockholders. What we are doing is bringing suit as trustee of the bankrupt because of title given to us by Section 70 (a) to, first, property belonging to the bankrupt but transferred by him in fraud of his creditors, and that certainly was done here; and, secondly, title to property which was unlawfully taken by the bankrupt—or from the bankrupt.



The Court: Now let me ask you about that next section. You say that you have that title under 70 (a). What property do you have the title to?

Mr. Teiser: Title to the particular property which was taken away from us. [10]

The Court: Where is it?

Mr. Teiser: Why, I suppose it has been disposed of by Mr. Farrington. If I recall aright, right on the sudden spur there, if I recall aright, Farrington acquired the stock—the first time, he acquired stock of the Western Guaranty Company. He acquired stock of the Western Guaranty Company. That stock was disposed of by him. At least, we haven't found that he has it.

The Court: Well, after he disposed of it did the bankrupt have any title to it?

Mr. Teiser: The property itself?

The Court: Yes.

Mr. Teiser: It would have if the person to whom it was disposed of had knowledge of its origin and the stocks of it, and so forth, I suppose. But that is not the theory which—we are not claiming that he had. I see what your Honor means, but we are not claiming that.

The Court: The bankrupt didn't have title to the property, and therefore you didn't have.

Mr. Teiser: Oh, he had title at the time of its acquisition?

The Court: Yes.

Mr. Teiser: But at the time of the bankruptcy——

The Court: But at the time of the bankruptcy

the bankrupt didn't have title to it, and therefore you didn't have it.

Mr. Teiser: No, sir, but Section 70 doesn't say that he has [11] title to the property. Section 70 (a) says title to property transferred by him in fraud of his creditors.

The Court: That is an ungodly right, because if the bankrupt didn't have title to the property at the date of the bankruptcy then the trustee didn't get it.

Mr. Teiser: No, we didn't have title to the property. We had title to a cause of action to recover that property.

The Court: Yes, that is just what I am trying to get you down to: The bankrupt didn't own the property, the trustee didn't own the property, and what you had title to was a cause of action which did belong to the bankrupt and which you inherited.

Mr. Teiser: I won't go as far as that, your Honor. I think the bankrupt did have title to the property. At least he did have title to the property unless the person who acquired the property——

The Court: You don't even claim in your complaint or any place in this lawsuit that he had title to the property.

Mr. Teiser: We don't.

The Court: No.

Mr. Teiser: We don't claim it now. We are not suing for title to the property.

The Court: Well, in other words, you are getting down to a position where Section 70 (a) doesn't do you a bit of good.

Mr. Teiser: I can't see that, if your Honor please.

The Court: Well, you tell me how that would do you some good. [12] That is what I am trying to find out.

Mr. Teiser: I am trying to, your Honor, as best I can, and there must be something faulty with me that I can't make my position clear.

The Court: No, there is something faulty in me because I can't understand you.

Mr. Teiser: Well, maybe it is both of us. That section says, "The trustee of an estate of a bankrupt shall be vested by operation of law with the title of the bankrupt to all property transferred by him in fraud of his creditors." Let's take that one piece alone: He is "vested by operation of law with the title of the bankrupt to all property transferred by him in fraud of his creditors." "Transferred by him in fraud of his creditors"—now, what could that mean? It could only mean that property which had already been transferred in fraud of his creditors,—he has a right to title to that property.

The Court: But he hasn't. You have already said that the bankrupt——

Mr. Teiser: The Act says that he has.

The Court: No, it doesn't. It says "the title of the bankrupt." Now, if the bankrupt had no title, obviously a trustee doesn't get anything.

Mr. Teiser: No, "vested by operation of law with the title of the bankrupt to all property transferred by him."

The Court: But if the bankrupt didn't have title to property [13] transferred in fraud of its creditors, obviously the trustee doesn't get anything. Now, if property is transferred in fraud of creditors——

Mr. Teiser: Now, wait a minute. Maybe I see what you are talking about. You said that the title of the bankrupt to property transferred in fraud of his creditors—title of the bankrupt to property transferred in fraud of his creditors. Naturally, if a bankrupt transfers property in fraud of his creditors, the bankrupt, you can well say, hasn't the title to that property ever, could never have, because, having transferred it, the bankrupt having transferred property in fraud of his creditors, could never recover it back, because that is his act and consequently he couldn't recover it back; but the Bankruptcy Act says—it gives him a new life, gives the trustee a new life, it gives him the title of the bankrupt in property which the bankrupt has transferred in fraud of his creditors, which could not have been given to him at the time prior to bankruptcy, because the bankrupt couldn't recover property which he transferred in fraud of his creditors, unless in a circumstance such as this someone fraudulently and improperly caused it to be done, then you bring suit against the person who fraudulently caused it to be done.

Then you come to the second section, which provides that he acquires the title of the bankrupt to "rights of actions arising upon contracts or from

the unlawful taking or detention of, or injury to his property.”

Now, under either one of those, under (4) or (6), I [14] say we have acquired rights to this property or to the damages for the taking of the property, and under section (6) we obtained title to a claim to the property arising by virtue of the detention of or taking of the property.

The Court: If the bankrupt transfers property in fraud of his creditors, that is a voidable transfer.

Mr. Teiser: Yes.

The Court: Against certain persons.

Mr. Teiser: It is also a voidable transfer, yes, sir.

The Court: No, it is a voidable transfer. It isn't also a voidable transfer,—it is a voidable transfer as against a creditor in judgment of an execution returned unsatisfied or, in the instance of a corporation, against a new director.

Mr. Teiser: Oh, we don't even have to have a judgment—well, I won't go into details on that, your Honor.

The Court: Well, that is a common law rule, I am saying.

Mr. Teiser: Under the Bankruptcy Act the mere transfer in fraud of creditors—

The Court: I am just talking about the bankrupt,—the bankrupt's title is there, but voidable under certain circumstances. Now, then, if the assignee in fraud of creditors makes a transfer to a purchaser in good faith and for value, then the bankrupt has no title.



Mr. Teiser: Has no title to the property, but he has title to the right—— [15]

The Court: That is just the point I am making now. I am trying to get you so the point is clear, that you recognize that there is a difference between the title to the property and the title to the cause of action. After the assignee in fraud of creditors has himself sold the property to a bona fide purchaser for value, then the bankrupt has no title whatsoever, or the transferor in fraud of creditors has no title whatsoever to the property.

Mr. Teiser: At least, he couldn't recover it, I will say that.

The Court: No, he has no title.

Mr. Teiser: Probably has no title to it, because if he couldn't recover it it wouldn't do him any good to have title to it.

The Court: Well, I just say he has no title to it.

Mr. Teiser: Well, I will just say I will go along with you.

The Court: That is what I am trying to get you down to. If that isn't a valid position, I want you to show me why, and, furthermore, I want you to bring me some authorities. Now, I have made extensive search on this subject, but I have found no authority that supports the position that he has any title.

Mr. Teiser: Title to the property, you are speaking of?

The Court: Title to the property. He still has a cause of action. The bankrupt—for instance, a



bankrupt corporation—or the transferor in fraud of creditors is in the position of [16] the corporation, and the transferor still has a right of action against the transferee.

Mr. Teiser: I think that is right, and I think this section (6) was put in the Act because they didn't want somebody to come in and claim that because the property happened to be transferred to a bona fide purchaser for value and couldn't recover for that reason, that he couldn't recover damages for the same.

The Court: All right, now——

Mr. Teiser: I think I tried to set that forth in pages 2 to 6 of my brief. Maybe I didn't do it very clearly.

The Court: All right,—I wasn't sure that we were on the same ground. That is the thing I am trying to find out, whether we are on the same ground.

Mr. Reilly: Why, it has seemed to us all along, your Honor, that counsel has switched theories. The whole of the pre-trial order is based upon the proposition that the statute of limitations is two years from the time of discovery or the time when the alleged fraud should have been discovered. That is stated in plaintiff's contentions. The last paragraph of his contentions is that "This plaintiff brought suit within two years of the discovery of the fraud set forth in the first and second claims herein." Then the issues of fact which are to be tried—well, all of the issues of fact,—they are listed on page 24 of the pre-trial order, and they

are, Did the plaintiff have actual [17] knowledge within two years—more than two years, or should he have had knowledge of both transactions? and the issues that are submitted for trial are stated at page 25 of the pre-trial order similarly, and page 26; so that the issue that we came to try before your Honor was a two-year statute of limitations. At the trial no farther or no different theory was advanced other than that two-year statute of limitations, and your Honor stated the rule, with agreement of counsel to it, thus, at page 156:

“The Court: The objection is overruled. I might explain to you I don’t think it makes any difference what you knew, if, being charged with this duty to investigate and bring an action, there was at hand information which pointed fairly directly to this matter, and that is the basis on which I am considering the materiality.

“Mr. Teiser: I think that is the proper basis, your Honor.”

Then in his opening brief he again affirms that position.

Now, as far as his proceeding under 70 (a) or 70 (e) or 67 is concerned, to us it doesn’t make a great deal of difference, because the State statute is applicable in any event, under the authorities. So there doesn’t seem to be any particular distinction between 70 (a) and 70 (e).

Collier says, at page 1591:

“The trustee under 70 (e) must establish the existence of all facts which were essential under the state law to authorize recovery by a creditor to lose

right of action of trustee as subrogated. In view of the wide scope of (e), it appears that the provisions of (a) (4) are unnecessary. If the trustee proceeded only in reliance on (a) (4) he would have to establish that the property he sought had been conveyed in fraud of creditors and then assert by [18] clause (4) it was vested in him. That is precisely what he can accomplish under (e)."

The statute of limitations, as we understand it, in any event, is the two years from the discovery or from the time it should have been discovered. Now, that is the theory under which the pre-trial order was formed, it is the theory upon which the case was tried, it is the theory of the questions which were submitted to your Honor for trial, and——

The Court: I don't think it is as simple as that, Mr. Reilly. I think it still has to consider the question of the statute of limitations as introduced in the Chandler Act. I don't think you can escape that.

Mr. Reilly: Well, on that point, your Honor, our view is this, that the statute of limitations had run prior to the Chandler Act in 1938. The right of the defendant not to be sued and become vested could not be constitutionally taken away from him. We haven't cited cases on that in our brief. I had that in mind, and, of course, was ill at the time. I have some cases now, if your Honor would care to have them submitted.

The Court: Well, I am trying to keep the discussion limited, because I may say I have fully

made up my mind, just as soon as I get this filed down so that I know what the plaintiff is talking about.

Mr. Reilly: Yes.

The Court: I was confused to some extent by the way that the briefs failed to hitch right in my mind. [19]

Mr. Reilly: Well, then, secondly, that is, in addition to the vested right of the defendant in the statute which had already run, we say that the Chandler Act having been postponed in its operation for several months,—I don't remember the number of months now—that that, under the very great weight of authority, not including New York, which counsel cited, which is in the minority, that that act is to be construed to act retrospectively, the time of postponement of its going into effect being the time allowed for the bringing of pending cases.

The Court: Well, that doesn't necessarily apply to a cause of action which arises under the Bankruptcy Act itself, rights given to the trustee by the Bankruptcy Act itself and not inherited.

Mr. Reilly: I think it does, your Honor.

The Court: And not inherited?

Mr. Reilly: I think it does, because the Act, the Chandler Act, if it confers any rights, in the same statute conferred limitations on those rights. It really is not a statute of limitations, but it is a limitation on the right itself, therefore it applies to everything created by the Chandler Act, and the limitation of two years after the adjudication, in

our judgment, applies to every action which the plaintiff can assert under the Chandler Act. That is our contention on that, your Honor.

The Court: Well, the Herget case, of course, deals with that, in that recently announced opinion of the Supreme Court [20] of the United States.

Mr. Reilly: The what?

The Court: The Herget case.

Mr. Reilly: Yes.

The Court: Herget vs. the Central National Bank.

Well, have you any further comment to make as to Mr. Teiser's now definition of his position?

Mr. Reilly: Well, I think he is going to come under 70 (e), in any event, or 67.

The Court: Well, I don't care to have your analysis of it. He has stated now pretty definitely where he thought his cause of action arose.

Mr. Reilly: Yes.

The Court: And how the trustee got hold of it.

Mr. Reilly: Yes.

The Court: By operation of law, under the Bankruptcy Act, he acquired a right which had previously existed in the bankrupt. Do you see anything more in it?

Mr. Reilly: I understand that to be his theory, yes.

The Court: And that is the idea upon which we are proceeding?

Mr. Reilly: Yes, your Honor, I think that is.

The Court: All right. Well, as I say, I have made up my mind in this case, and I determine it,



with that clarification, I determine the case in favor of the defendant. I have discussed this question—I have an opinion which is about ready, but I [21] wanted to clear this up, because I had, to a certain extent, still misconceived the attitude of the plaintiff, and I assumed that it was a right of action arising in creditors and inherited by the trustee. I am going to change that discussion of that to say that it is a right of action which arose in the bankrupt and was inherited, by operation of law, by the trustee. In the discussion of that point, now that we are talking about it,—yes?

Mr. Teiser: Why, I don't want to say anything to interrupt your Honor. I just hope that it won't be taken that that was my view as you just expressed it, by me saying nothing. If you want me to say what I meant, I will be very glad to do so.

The Court: Well, I have been sitting here for half an hour trying to get you to say what you meant.

Mr. Teiser: Well, I tried to say it, and I think you made a statement there that I don't agree with.

The Court: Well, we have talked in this record now for pretty near an hour, and the thing that you have said over and over and over again is that this was a cause of action which subsisted in the corporation and arose in it by virtue of the transactions which happened before the bankruptcy and was thereafter inherited by the trustee.

Mr. Teiser: If your Honor please, I agree that I said that, but I didn't say that it wouldn't be a cause of action which the bankrupt didn't have,



that the trustee would have had. I [22] tried to say that once before, that even though the bankrupt himself could not bring this suit the trustee could, because the bankrupt may have been precluded, because of his action, from ever bringing this suit, and the trustee could bring it. Now, the only derivative cause of action that I know of—I mean the only cause of action given by the Bankruptcy Act itself that I know of and not giving rights to the trustee is a cause of action for preference. Now, if the Bankruptcy Act meant that the only suit which a trustee could bring within two years after the—the former Bankruptcy Act—after his dismissal, after his discharge, why didn't they say that actions for preference should have been brought?

The Court: I am not talking about all the rest of them. I am talking about this one. Now, how do you say that the trustee got the right to bring the cause of action that didn't subsist in anybody before the time that he was appointed?

Mr. Teiser: I say that even though the bankrupt could not have brought this action——

The Court: Well, am asking you what provision of law you base that idea on?

Mr. Teiser: 70 (e)—70 (a).

The Court: Yes. I have already pointed out to you, and you have admitted, that he didn't have any property, and could not have had any property, in these specific titles, and that you weren't suing for it. [23]

Mr. Teiser: Well, under Section 70 (a) that is

—well, pardon me, your Honor, you have already decided the case. I certainly don't want to, and could not at this time,—

The Court: No, I am not asking you to say anything about my decision of the case. I am trying to decide this case directly,—

Mr. Teiser: I know you are.

The Court: —and decide it on the theories that you have advanced, and not on anything else, and if you can show me any provision of law, now, that says that this is not a derivative action, not an inherited action, I will consider it.

Mr. Teiser: Your Honor, the only difficulty between you and me is that I think your Honor feels that that is not an action which was given under the Bankruptcy Act. Now, that is the only difference between us, and yet it must be interpreted, and you are the one to interpret it, that is all. I maintain that under Section 70 (a) a cause of action is given to the trustee—a cause of action is given to the trustee—that the bankrupt may not—in some instances could and in many instances could not—that is the difference between 70 (e) and 70 (a): in many instances could not have brought the suit, in many instances.

The Court: I realize he could not have brought the suit, but the law doesn't say anything about that. It says "property of the bankrupt".

Mr. Teiser: Your Honor is not giving sufficient credit, I [24] don't think, to Section 70 (a) (6).

The Court: Yes, that refers to an entirely different thing. That refers to property that was

wrongfully taken and withheld from you,—in other words, a replevin case.

Mr. Teiser: Oh, I don't think that would be a replevin case.

The Court: All right, there is no authority to the contrary. Well, in any event, whether it be one thing or the other, I assume that this was as I have stated it.

I am going to read this as now amended:

“There can be no question that the claimed right of action arose in the bankrupt corporation or in the trustee and was inherited by the trustee. It does not take its initial genesis by virtue of the provisions of the Bankruptcy Act. Before the passage of the Act of 1938 it had been consistently held in the Ninth Circuit that to such an inherited cause of action the general statute of limitations prescribed by the particular state applied. This was the more logical, since it is a principle agreed upon with unanimity that where a right of action given by a particular state was conditioned in the same statute by a limitation the expiration of the period thus set would bar the remedy, notwithstanding the language of the old clause 11 (d). Universally the Courts maintain that where the general law of the state had provided the right in a creditor, if the law of general limitation set up by the state had barred the remedy in the creditors the trustee could not revive it. [25] This was founded upon the proposition that the trustee was enforcing a right based upon rights inherited from the bankrupt or the creditors and for which reme-

dies were given by state law. It has been intimated that the former provisions of the Bankruptcy Act had no effect upon this situation, since former Section 11 (d) was a withdrawal of juridical and representative capacity, therefore, that section was not intended as a statute of limitations but simply a termination of power. There were, it is true, cases holding that old Section 11 (d) was a true statute of limitations, and if the remedy of a creditor were alive on the date of filing of the petition it lingered on available to the trustee until two years after final closing."

Now, in that note I cite *Callaghan vs. Bailey*, 293 N. Y. 396, which is cited in the *Hastings* case.

"But practical considerations as well as authority constrained this Court to the opposite view. Repose is the aim of these local statutes, and the state policy should control. While, then, a case can be made for the retention of the remedy until a trustee could orient himself before bringing action, it should not be extended, as in this case, to thirteen years, unless the affirmative policy of the state permit."

The Court thereafter—I am not going to read the whole opinion—the Court thereafter holds that the statute had run and that there was an actual discovery or that the trustee knew sufficient facts so that he should have known of the existence [26] of the cause of action, and the Court as a subsidiary ground uses the ground of laches as far as the trustee was concerned. I did say in that regard, "The trustee and the present attorneys have de-

voted years of unflagging zeal to obtain recoveries in the Bank of California case, but it is the opinion of the Court that they deliberately spent their work and efforts upon that proposition as the main chance and that they did not as vigorously pursue the clues that might have led to a like recovery in the instant cause. There were sufficient facts of record long ago to have accomplished this purpose", and I discussed that to a further extent.

Now, with regard to Sections 70 (a) and 70 (c), I say, "These are not antagonistic, as contended for by plaintiff. By subsection (a) the trustee acquired all the rights which the bankrupt had in property which he transferred in fraud of creditors. By the former Section 47(a) (2) the trustee was given the rights of creditors as to all the property with which he became vested by virtue of the clauses of Section 70. In the Act of 1938 all these provisions now become a part of Section 70 and the causes of confusion no longer exist.

"The judgment will be that the statute of limitations has run against the cause of action and that subsidiarily the trustee has lost the right by virtue of laches."

Mr. Reilly: There will be findings?

The Court: I will give you a formulated copy of the opinion [27] as soon as it is run off, now, and thereafter you can present findings.

Mr. Reilly: Very well, your Honor.

The Court: Court is in recess until two o'clock.

(Thereupon, at 12:33 o'clock P. M., March 30, 1945, proceedings herein were concluded.)



[Title of District Court and Cause.]

CERTIFICATE

I, Cloyd D. Rauch, hereby certify that on March 30, 1945, I reported in shorthand certain proceedings had in the above entitled court and cause, that I subsequently caused my said shorthand notes to be reduced to typewriting, and that the foregoing transcript, pages numbered 1 to 28, both inclusive, constitutes a full, true and accurate transcript of said proceedings, so taken by me in shorthand on said date as aforesaid, and of the whole thereof.

Dated this 28th day of June, A. D. 1945.

CLOYD D. RENCH

Court Reporter.

[Endorsed]: Filed July 28, 1945. [29]

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[Endorsed]: No. 11116. United States Circuit Court of Appeals for the Ninth Circuit, George M. McBride, Trustee in Bankruptcy of Western Bond and Mortgage Company, an Oregon Corporation, Bankrupt, Appellant, vs. C. H. Farrington, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the District of Oregon.

Filed August 3, 1945.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals  
for the Ninth Circuit.



In the United States Circuit Court of Appeals  
Ninth Circuit

No. 11116

GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond & Mortgage Company, an  
Oregon Corporation, Bankrupt,

Appellant,

vs.

C. H. FARRINGTON,

Appellee.

STIPULATION

It is stipulated by the appellant, through his counsel, Sidney Teiser, Esq., and by the appellee, through his counsel, John F. Reilly, that Exhibits Number 63, 65, 73, 76, 78, 83 and 84 are copies of newspaper articles appearing in the newspapers as shown on said exhibits and that the same newspaper articles clipped from the respective newspapers designated on said exhibits were among other newspaper articles and other memorandums and documents contained in a credit file of the Bank of California which is Exhibit 162 herein and which was an exhibit in the trial of an order to show cause against the Bank of California National Association, In the matter of Western Bond & Mortgage Company, a corporation, bankrupt, in Bankruptcy No. B16722 in the District Court of the United States for the District of Oregon, except that the newspaper articles as they appear in Exhibits Num-

ber 63, 65, 73, 76, 78, 83 and 84 do not contain headlines and in the articles as they appear in Exhibit 162 headlines are included.

It Is Further Stipulated, That Exhibits Number 89 to 102, both inclusive, are exhibits from testimony appearing and contained in Exhibits 103 and 103A (said exhibits 103 and 103A being a printed transcript of record in the case of Bank of California National Association, Appellant, against George M. McBride, Trustee in Bankruptcy of Western Bond & Mortgage Company, Appellee, Number 10062 in the United States Circuit Court Page 1—Stipulation of Appeals for the Ninth Circuit.)

It Is Further Stipulated by Appellant and Appellee herein that said exhibits herein mentioned, as well as all other exhibits transmitted by order of the District Court of the United States for the District of Oregon in their original form to this court may be considered in the appeal of this case as though copies of said exhibits were sent instead of originals, and this irrespective of whether or not any or all of said exhibits be printed in the transcript of record in the appeal in this cause.

Dated at Portland, Oregon this 25 day of July,  
1945.

SIDNEY TEISER,  
Attorney for Appellant

JOHN F. REILLY,  
Of Attorneys for Appellee.

So Ordered.

FRANCIS A. GARRECHT,  
Senior United States Circuit  
Judge

[Endorsed]: Filed July 27, 1945. Paul P.  
O'Brien, Clerk.

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[Title of Circuit Court of Appeals and Cause.]

CONCISE STATEMENT OF POINTS IN  
WHICH APPELLEE INTENDS TO RELY  
ON THE APPEAL AND DESIGNATION  
OF RECORD

I

Plaintiff below had two years after closing of  
the estate within which to sue, and thus suit was  
timely.

II

But if plaintiff had only two years from the  
time of the discovery of the fraud, this suit would  
still have been timely, since fraud was not dis-  
covered within two years previous to instituting  
suit.

III

And even if the Trustee had but two years from

the time when by reasonable diligence, the fraud alleged should have been discovered by him, still, this suit would have been timely, since the fraud could not, with reasonable diligence, have been sooner discovered.

#### IV

The Trustee was not guilty of laches.

#### V

Creditors should not be penalized because of the negligence of the Trustee, assuming the Trustee were negligent, and hence, even though the Trustee, through neglect, failed to discover the fraud, this suit was still permissible to be brought, and was timely begun.

### DESIGNATION OF RECORD

In the presentation of the above points, appellee designates all of the record transmitted by the Clerk below, under his certificate as the record on which he intends to rely.

Respectfully submitted,

TEISER & KELLER

SIDNEY TEISER

Attorneys for Appellant

United States of America,

State of Oregon

County of Multnomah—ss.

Due service of the within Points & Designation hereby accepted in Multnomah County, Oregon, by receiving a copy thereof duly certified.

JOHN F. REILLY,

Attorney for Appellee

Sept. 11th, 1945.

[Endorsed]: Filed Sept. 13, 1945. Paul P. O'Brien, Clerk.

At a Stated Term, to wit: The October Term 1945, of the United States Circuit Court of Appeals for the Ninth Circuit, held in the Court Room thereof, in the City and County of San Francisco, in the State of California, on Monday the nineteenth day of November in the year of our Lord one thousand nine hundred and forty-five.

Present:

Honorable Francis A. Garrecht, Senior Circuit Judge, Presiding,

Honorable Clifton Mathews, Circuit Judge,

Honorable William Healy, Circuit Judge.

[Title of Cause.]

#### ORDER ON MOTION FOR ELIMINATION OF ORIGINAL EXHIBITS FROM PRINTED TRANSCRIPT

Upon consideration of the motion of appellant for an order eliminating from the printed transcript of record the original exhibits in above cause, and of the objections of appellee thereto, both papers filed November 15, 1945, and by direction of the Court,

It Is Ordered that the original exhibits in above cause need not be printed as a part of the transcript of record, but that counsel for respective parties may print as an appendix to their respective briefs such portions of said exhibits as are relied upon, the cost of printing such appendices to abide the determination of the appeal herein.



In the United States  
**Circuit Court of Appeals**  
For the Ninth Circuit

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,

*Appellant,*

vs.

C. H. FARRINGTON,

*Appellee.*

---

**BRIEF OF APPELLANT**

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Upon Appeal from the District Court of the United  
States for the District of Oregon.

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SIDNEY TEISER,  
WM. G. KELLER,  
(Teiser & Keller)

*Attorneys for Appellants.*

FILED  
APR 4 1946  
PAUL P. O'BRIEN,  
CLERK



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In the United States  
**Circuit Court of Appeals**  
For the Ninth Circuit

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,

*Appellant,*

vs.

C. H. FARRINGTON,

*Appellee.*

---

**BRIEF OF APPELLANT**

---

Upon Appeal from the District Court of the United  
States for the District of Oregon.

---

**STATEMENT OF THE CASE**

A petition in bankruptcy was filed against the Western Bond and Mortgage Company on November 25, 1931 on which it was thereafter adjudged bankrupt. On December 4, 1934 George M. McBride, appellant here, was elected Trustee and thereupon duly qualified.

On October 2, 1943 the Trustee filed an action based on fraudulent appropriation by C. H. Farrington, the president of the bankrupt corporation, of assets of over half million dollars. This action is the subject of the appeal.

The issue was raised by Farrington, the appellee, that the suit was barred by the statute of limitations in that it was not brought by the Trustee within two years from the time the fraud should have been discovered.

The Oregon Statute limits the time when a suit may be instituted for fraud to two years from the discovery.

## **I. THE FACTS AS TO FRAUD, AND THE COVERING UP OF SAME.**

C. H. Farrington, appellee, was president of the bankrupt corporation and the owner of substantially all of its common and controlling stock. In December, 1930, less than a year prior to the bankruptcy, Farrington concocted a scheme, which he carried out, whereby assets of the corporation of large value was appropriated by him; and the corporation was denuded of these assets and received nothing of value in their stead. The method of manipulation whereby such scheme was carried out was the formation of a corporation, the transferring of assets to such cor-

poration and to other corporations controlled by Farrington and the exchanging of stock for property, with the result that ultimately, and through intermediate transfers, Farrington had acquired the property of the corporation paying nothing of real value therefor, and the corporation was left without such assets or other thing of value. The consummation of these fraudulent transfers were handled so that their real purport was not discoverable from the books and records of the bankrupt corporation. The method of handling the transactions were formulated and designed to prevent discovery.

The first of the two claims set forth in the complaint, for example, was handled in the following manner:

Farrington, the president and controller of the stock of the bankrupt, caused a corporation to be formed without authorization, which he called the *Western Guaranty Co.*, with \$5000 par value stock; and likewise without authorization, he caused the bankrupt corporation to subscribe for all of such stock, transferring to the Guaranty Co. assets of a value of \$322,014.35 for such stock of a \$5000 par value. Thereupon Farrington, through a dummy corporation owned by him personally, purchased for his worthless stock in the bankrupt corporation certain worthless stocks, notes and accounts, and simultaneously purchased from the bankrupt corporation the Guaranty Company's stock (representing its \$322,-

014.35 of assets) for these worthless securities. These transactions, however, in so far as they were recorded on the books or records of the bankrupt, showed merely a transfer of assets (\$322,014.35 of accounts and notes for Guaranty Co. stock) to a wholly owned subsidiary and then the transfer of that stock for property of equal value. Farrington's connection with these matters were not disclosed by the books.

The second of the two claims set forth in the complaint was handled in the following manner:

The bankrupt owned 40,000 shares of the Consolidated Credit Corporation's stock of a total value of \$120,000. Without any authority Farrington caused this stock to be transferred out of the bankrupt corporation to a person or persons unknown, in consideration of all the capital stock of the Keystone Finance Company, purporting to be of equal value. As a matter of fact, the stock of the Keystone Finance Company was then already owned by the bankrupt. However, its ownership of such stock was not disclosed by the books of the bankrupt.

## II. THE FACTS AS TO THE DISCOVERY.

It must be admitted that the Trustee did not discover the frauds set forth until a few months prior to the filing of the suit. Certainly if that fact is not conceded it is apparent that the evidence does not disclose any such actual discovery on the part of the

Trustee. On the contrary, the Trustee's testimony (Tr. pp. 95, 96) is a positive affirmation of the non-discovery of the facts.

### III. THE FACTS CONCERNING FAILURE TO DISCOVER.

#### (a) Western Guaranty Co. Stock Appropriation (The First Claim).

The Trustee was appointed in December, 1934. Early in 1935 the Trustee, upon authority of an order of the Referee (Exhibit 104, Tr. p. 120) employed John R. Latourette as attorney to represent him. Mr. Latourette acted as attorney for the Trustee for about a year. In 1936 the firm of Teiser & Keller was substituted for him as attorney for the Trustee. (Exhibit 106). During the year that the Trustee was represented by Mr. Latourette, according to Mr. Latourette (defendant's own witness):

"Well we investigated everybody we could from the time I was there, trying to get some assets. We investigated Mr. Farrington, the Bank of California—we had two accountants from the Corporation Department that were in my office a number of times and were in Mr. McBride's office. I was down there. I went through as many records as I could find that pertained to any of the people that were involved in the thing.

I think I was in there for about a year and we concluded that we had a case against the Bank of California, and I prepared a complaint, a rough draft, which I was waiting to submit to



Mr. Moody for his approval. I never got to see Mr. Moody or never prepared the complaint in its final form during the time I was representing the Trustee, I think about a year or more." (Tr. 208-210).

When he was asked what he discovered about any lawsuits which had been brought concerning the Western Bond and Mortgage Company and Mr. Farrington in 1931 and as to any discussion he had with the Trustee concerning them he answered:

"I don't know. I can't say definitely that he had any discussion with Mr. McBride about the particular suits. I know they were trying—we were trying to find out about the whole thing, about Mr. Farrington, as well as all of the others who had been involved in the thing, but as to any particular conversation regarding those things after these, so many years, I do not recall.

"Mr. Moody told them (the State Department's auditors) to cooperate with us and they were available to us at all times, and they had been through the records pretty thoroughly. It seems to me that they had made a general report—I might be mistaken about that though." (Tr. 208-210).

Upon the substitution of the present attorneys for Mr. Latourette these attorneys continued the investigation and discovered that notwithstanding nothing had been done about it the Bank of California transaction "stuck out like a sore thumb". (Tr. p. 213). Subsequently suit was instituted and recovery had against that Bank. From further investigations made by the attorneys another matter developed, viz., a



matter concerning transaction with Dr. Besson and Mr. Brown, and this matter was litigated (Tr. p. 213). Another situation also arose and was investigated, viz., transfer of property in Corvallis (Tr. p. 213) though no recovery was made as to the latter.

Mr. McBride during the period of his trusteeship, particularly in the first year thereof, had the assistance of the Assistant Attorney General of Oregon, Mr. Ralph E. Moody, and certain auditors from the Corporation Commissioner of the State of Oregon, and both Mr. McBride and these auditors made investigations, but it is quite apparent that no information was obtained either by Mr. Moody or the auditors concerning the facts set forth in the Trustee's claims. (Tr. p. 104 and pp. 193, 194).

The Trustee himself it appears was not an accountant, though he had some knowledge of bookkeeping, and he himself examined the books (Tr. p. 108) and found nothing irregular. (Tr. p. 96).

As a preliminary to bringing the proceedings against the Bank of California, the Trustee in 1936 employed Rudolph Erickson, a certified public accountant (Tr. p. 122) for the purpose of making a general investigation of the books, (Tr. p. 168) but particularly in reference to matters connected with the bankrupt's transactions with the Bank of California. (Tr. pp. 175, 176). Mr. Erickson found that the books on their face showed no improprieties in regard to transactions concerning the transfer of the

Western Guaranty Co.'s stock (Tr. p. 141). In June of 1943 the accountant first discovered the questionable character of this transaction. (Tr. pp. 144-145 and p. 148).

The occasion resulting in the discovery arose under the following circumstances:

In 1935 the United States Government filed a claim for additional income taxes claimed to be due for the year 1930 (Tr. p. 91). Shortly after the filing of the claim the Trustee called on the then Referee, Mr. A. M. Cannon for the purpose of discussing with him the making of objections at that time to the Government's claim. (Tr. p. 91). He was told by the Referee that there was no purpose to be served by filing at that time objections to the Government's claim since the estate had no money in it with which to pay any portion of the claim even if it were allowed, and the matter would therefore be merely academic at least until such time as property or funds should come into the estate out of which the claim could be paid. (Tr. p. 92). So the Referee instructed the Trustee, until further advice, not to file objections to the claim (Tr. p. 92). In 1943 the first money or property came into the estate over and above the amount deemed necessary to pay the expenses of administration. (Tr. p. 93). At that time, pursuant to instructions given by the Referee, who was then Mr. Estes Snedecor, it was determined to investigate the claim of the Government for the purpose of determining what, if any, objection should be filed to such claim.

(Tr. p. 93). The claim of the Government was for over \$50,000 and, with interest, amounted to approximately \$65,000. (Tr. p. 120). With the approval of the Referee, the Trustee re-employed certified public accountant Erickson (Tr. p. 87 and pp. 176, 177), this time for the purpose of making an examination in the endeavor to discover data on which to file objections to the tax claim. (Tr. p. 94). Concomitant with the employment of Erickson the Trustee attempted to obtain, upon Erickson's suggestion, a copy of the original report of the revenue agent upon which the additional assessment of 1930 income tax was based. (Tr. p. 94). The Trustee had endeavored to obtain a copy of this report prior to the time he had the discussion with Mr. Cannon, the former referee, but in the light of Mr. Cannon's determination that the tax claim need not then be contested, the Trustee made no further effort to obtain a copy of the report until ~~1934~~ (Tr. 119, 120) when the contest over the claim became imminent. There was no copy to be found in the records of the Western Bond and Mortgage Co. (Tr. p. 146) and the Trustee had never seen a copy of it (p. 119) until a short time before the present suit was brought. A copy of the report (Exhibit 59) was ultimately obtained from the Internal Revenue Department in 1943 (Tr. p. 146) and such copy was turned over by the Trustee to the Certified Public Accountant so that the accountant could have before him the basis on which the additional tax was assessed. The report not only showed such basis but

also indicated certain improprieties in connection with the Western Guaranty stock transfer. By reason of the lead thus furnished the certified public accountant brought the matter to the attention of the Trustee and was asked to make a thorough investigation and to report on the situation. (Tr. p. 147). The investigation thus made resulted in a report from which the facts set forth in the complaint were first discovered. (Tr. p. 96). When the accountant's report was made to the Trustee the Trustee made immediate additional efforts to confirm the facts reported. This he did, by causing the accountant and his attorney to make two trips to Seattle and Everett, Washington, and to confer with those having information there (Tr. p. 151) and by causing examinations to be made of various parties under the provision of Sec. 21(a) of the Bankruptcy Act. (Tr. p. 95). Upon thus verifying the data contained in the report of the certified public accounts, the Trustee filed a suit which is the subject of this appeal.

**(b) Consolidated Credit Corporation Stock  
Transfer (The Second Claim).**

The accountant ascertained the facts in the Consolidated Credit stock manipulation in connection with the seeking of valid offsets to the alleged profits asserted by the Government in the maintenance of its claim for additional taxes. Naturally the Government did base its claim on the Revenue Agent's re-

port and naturally the accountant did need that report in his examination in connection with the Trustee's opposition to the Government's claim. But until the claim of the Government was being pressed by it in 1943 and until the Trustee was required to prepare for trial in opposition to such claim there was no need for an inspection of the Government Agent's Report, nor was there any earlier need to delve into the claim of the Government in an effort to defeat the tax. Let it be said in this connection that the Revenue Agent's report made no mention whatsoever of the Consolidated Credit Corporation's stock manipulation. It was discovered by the certified public accountant in the following manner:

Items of profit reported by the Revenue Agent, as well as other transactions shown by the Company's books were scrutinized by the accountant not only for the year 1930 but for the year 1929. It was necessary to examine the 1929 transactions since the Company had the right of a deduction in 1930 for carry-over of a 1929 loss. In the Revenue Agent's report for the year 1930 (Schedule A of its Exhibit 5-A) the Revenue Agent made an adjustment increasing the taxable income for 1930 through a decreasing of the allowable deduction for the loss carry-over for 1929. In the accountant's research for available offset he had to examine many and varied transactions found on the Company's books. Most of the transactions, upon examination, were deemed to be of no available use either for the purpose of offsetting the additional



profits asserted by the Government Agent, or the deductible losses negated by the Agent, but some were found which seemed to be available. However, even as to those which seemed to be available some upon further search were found not to be and others were found to be. Among the latter there was discovered by the accountant a sale appearing on the books of 40,000 shares of stock of Consolidated Credit Corporation made in 1929 for 1500 shares of the Keystone Finance Company's stock. (Tr. p. 178). In considering the acquisition of the 1500 shares of the Keystone Finance Co. by the Western Bond and Mortgage Co. the accountant endeavored to trace from whom those shares came. He went to the minute books of the Keystone Finance Co. and found that the shares were subscribed for in the name of one Tapfer and one Snodgrass (Tr. p. 181), in consideration of the transfer by Tapfer and Snodgrass of the property known as the Russell Ranch in Crook County, Oregon. (Tr. p. 181).

Now it so happened that the accountant at the time of this examination in 1943 had in his possession an abstract of title to the Russell Ranch, since a client of his had just purchased such ranch from the Trustee. (Tr. p. 147 and 181). On the inspection of the abstract of title he ascertained that Tapfer and Snodgrass never owned this ranch, but that it was owned at that time, as well as prior and subsequently, by the Russell Land and Livestock Co., which had found to be a wholly owned subsidiary of the Western



Bond and Mortgage Company. (Tr. p. 148 and 181). Thus discovery was first made by the accountant (Tr. p. 148) that in 1929 the Western Bond and Mortgage Co. had parted with 40,000 shares of the Consolidated Credit Corporation's stock, which it owned, for 1500 shares of the Keystone Finance Co., which at that time it also owned (Tr. p. 178) and that therefore the bankrupt had parted with \$120,000 worth of property and receiving nothing therefor, it had sustained a loss in 1929 of \$120,000 on this purported transaction. Such a loss was offsettable for tax purposes against the Company's 1930 gain. This discovery having brought to the knowledge of the accountant facts which indicated that the Western Bond and Mortgage Company had parted with substantial assets for which it had received nothing, he promptly reported same to the Trustee, who promptly thereafter instituted the suit which is the subject of this appeal.

#### **IV. THE EXCUSE OR LACK OF EXCUSE FOR FAILURE TO DISCOVER.**

##### **(a) Farrington's Contentions.**

The contention is made by Farrington that the Trustee was negligent in his search for facts and that—as an ordinarily prudent man—he should have discovered Farrington's fraud earlier.

Farrington asserts three reasons why the Trustee's failure to discover his frauds, barred this suit:

First, he asserts that newspaper articles (Exhibit 162) had come to the knowledge of the Trustee and his attorney while they were taking testimony in the proceedings against the Bank of California and against Besson and Brown in November, 1936, and that these articles contained references to a suit against Farrington, the Western Bond and Mortgage Company, and others, and to two suits against the Western Bond and Mortgage Company. Such suits it is claimed by him were based on fraud, and that therefore had the Trustee searched into the records of these cases they would have led the trustee to further investigate, from which investigation, it is charged, the facts of Farrington's misdeeds as detailed in the present action would have been ascertained.

Second, the contention is made by Farrington that the Trustee was derelict in his failure to procure earlier than he did the Revenue Agent's Report (Ex. 59) on the additional tax liability of the bankrupt corporation for the year 1930. Had he procured this agent's report sooner, it is asserted by Farrington, the Trustee would at the time of such procurement been charged with a duty further to investigate and would have earlier been enabled to discover Farrington's fraud.

Third, Farrington further charges that the Trustee should have earlier caused to be made a complete examination of the books and records of the bankrupt.

**(b) The Trustee's Position.**

The Trustee maintains that his activities in connection with the discovery of Farrington's fraud was those of an ordinarily prudent man under the circumstances. He insists that, considering the method adopted by Farrington in manipulating the books to disguise the real purport of transactions and thus to prevent discovery, he discovered the fraud at the first occasion indicating its whereabouts.

The newspaper articles (Exhibit 162) had they sent him to the records of the cases therein referred to, he affirms, would have disclosed only one case against Farrington, and that would have further disclosed that that case had been dismissed by the one who had brought it and at his substantial taxed costs. The cases against the Western Bond and Mortgage Co. and others would have disclosed nothing in connection with the incidents here under review. No dereliction, therefore, he avers, could possibly have been predicated upon a failure to explore in this regard.

As to the asserted failure to obtain a copy of the Revenue Agent's report on 1930 taxes—(Exhibit 59) the only apparent reason for the obtaining of such report would have been in an effort to defeat, in whole or in part, the additional tax assessment based thereon. The Trustee insists he obtained this report immediately the defeating of the tax became an issue.

Of course a complete and thorough examination and audit by certified public accountants, in addition to the examination and report of the two state auditors, could have been made at the inception of the trusteeship or at any time thereafter. Whether such audit would have uncovered what was uncovered by the Revenue Agent, who had access not only to books and records of the bankrupt but to those of all other corporations, firms and individuals, is unknown. However, there was no moneys available with which the Trustee could pay for same. Until the payment of the Bank of California judgment in 1943 never was there more than \$2500 on hand at any year's beginning or end (Exhibit 111) and the average amount was much less.<sup>1</sup> This money had been ear-marked, in effect to defray the costs and expenses of carrying on the Bank of California litigation—the one which the Trustee's attorney stated "stuck out like a sore thumb". Until that litigation was brought to a successful conclusion no additional money was brought into the estate. (Exhibit 111).

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<sup>1</sup>An analysis of the financial report which is in evidence (Exhibit 111) shows that on December 31, 1934 there was no balance. On the same date in 1935 there was a balance of

	\$ 439.30
1936 .....	237.03
1937 .....	228.10
1938 .....	2,421.61
1939 .....	2,096.36
1940 .....	1,935.06
1941 .....	1,829.31
1942 .....	1,345.25
1943 .....	1,445.25

Hind-sight, *ex post facto* wisdom, clairvoyance, is not a required attribute of a trustee, and the lack of it is not to be used against him by one whose fraud was not earlier discovered.

It is further maintained that even were the Trustee negligent, his dereliction should not be callipered against the positive fraud of Farrington, to the detriment of innocent creditors who were injured by such frauds, and who were powerless to appraise or command the sleuthing faculties of the Trustee.

Moreover, the Trustee stresses the fact that there was no evidence adduced that any of the thousand creditors, even those who instituted suits against the corporation or against Farrington, ever call to his attention the frauds here presented.

## JURISDICTION

The District Court had jurisdiction of the cause by virtue of Sec. 67 (e) of the Bankruptcy Act (11 U.S.C., Sec. 107 (e) ), as amended, which provides that courts of bankruptcy as well as state courts shall have jurisdiction of such actions as here brought. Like jurisdiction is given under Sec. 70(e) (3) of the Act, (11 U.S.C.A. Sec. 110 (e) (3)—1945 Pocket Part).

This Circuit Court of Appeals has jurisdiction on appeal by virtue of Sec. 24(a) of the Bankruptcy Act, as amended (11 U.S.C.A. Sec. 47(a)—1945 Pocket Part).

## THE ISSUES

- I. Does the Bankruptcy Act of 1898 (prior to Amendment by the Chandler Act, apply?
- II. If so, does the Oregon Statute of Limitations (2 years from discovery,) or Sec.(d) of the Bankruptcy Act (2 years from the closing of the estate) apply?
- III. If the Applicable Statute is the Oregon Statute of Limitations, was the action brought within the time prescribed by that Statute?
- IV. Was the Trustee guilty of laches?

## SPECIFICATIONS OF ERRORS

- I. The Court erred in determining that the Oregon Statute was the Applicable Statute.
- II. The Court erred in determining that the time prescribed by the Oregon Statute, (if that Statute was the applicable one), had run before the institution of the action,
  - (a) In that it held that the Trustee had not brought the action within two years from discovery.
  - (b) In that it held that the information which came to the Trustee charged him with the duty to pursue it.



- (c) In that it held that such information, if pursued, would have resulted in discovery at a time more than two years prior to the institution of the action here.

III. The Court erred in holding that the Trustee was guilty of laches.

### SYNOPSIS OF THE ARGUMENT

- I. The Bankruptcy Act of 1898 (prior to Chandler Amendment) applies, and the limitation of Sec. 11(d) keeps the action alive until two years after closing of estate.
- II. If the Bankruptcy Act, as amended by the Chandler Act, applies, or if the Oregon Statute is the applicable statute, the action is not barred, because:
  - (a) The action was brought within two years of the discovery of the fraud.
  - (b) The Trustee had no information charging him with the duty of further inquiry.
    - (1) Knowledge of the newspaper articles was not such information.
    - (2) Knowledge of the availability of the books and records of the bankrupt was not such information.
    - (3) Knowledge of the existence of a Reve-

nue Agent's Report recommending additional assessment for 1930 tax was not such information.

- (c) But if Trustee were chargeable with duty of further inquiry, investigation in that one debatable instance, would not have resulted in discovery.
- (d) Discovery, even if made, would have related only to Trustee's first claim (the Guaranty Company stock transaction).
- (e) The negligence of the Trustee (if there was such) is not to be nicely balanced against the fraud of a defendant who fraudulently profited at the expense of innocent creditors having no authority over the Trustee nor any power to direct his activities.

III. There were no laches.

IV. Some comments on District Judge's Opinion.

### APPLICABLE STATUTES

Sec. 11(d) of the Bankruptcy Act of 1898 (Title 11 U.S.C.A., Sec. 29 (d) ) not amended by the Chandler Act, reads as follows:

"Suits shall not be brought by or against the Trustee of a bankrupt estate subsequent to two years after the estate has been closed."

Sec. 11(e) of the Bankruptcy Act of 1898, as amended by the Chandler Act of 1938 (Title 11 U.S.C.A., Sec. 29(e) Pocket Part) reads as follows:

“A receiver or trustee may, within two years subsequent to the date of adjudication, or within such further period of time as the Federal or State law may permit, institute proceedings in behalf of the estate upon any claim against which the period of limitations fixed by Federal or State law has not expired at the time of the filing of the petition in bankruptcy.”

The Oregon Statute, Sec. 1-206, O.C.L.A., reads as follows:

“Within two years—An action for assault, battery, false imprisonment, for criminal conversation, or for any injury to the person or rights of another, not arising on contract, and not herein specifically enumerated, provided that in an action at law based upon fraud or deceit, the limitation shall be deemed to commence only from the discovery of the fraud or deceit.”

The Oregon Statute, Sec. 9-103, O.C.L.A., reads as follows:

“A suit shall only be commenced within the time limited to commence an action as provided in Chap. 2, of Title 1 of this Code. . . . In a suit upon a new promise, fraud or mistake, the limitation shall only be deemed to commence from the making of the new promise or the discovery of the fraud or mistake. . . .”

## ARGUMENT

### **I. THE BANKRUPTCY ACT OF 1898, PRIOR TO THE CHANDLER AMENDMENT IN 1938, IS THE APPLICABLE LAW.**

Sec. 11(d) of the Bankruptcy Act of 1898 (Title 11 U.S.C.A., Sec. 29(d) ), unamended by the Chandler Act, provides that the Trustee has two years after an estate is closed before he is required to bring suit. At the time of the filing of the petition in the matter of the Western Bond and Mortgage Company, Bankrupt, and at the time of the appointment of the Trustee in 1934, the Bankrupt Act of 1898 unamended, was in effect and it is maintained that under the Act the Trustee has two years after the closing of the estate in which to bring suits of action. In 1938 the Bankruptcy Act was amended by the Chandler Act, which provided that the Trustee should be required to bring suit within two years of the date of adjudication, or within the time limited by the Federal or State statutes. Assuming, but by no means admitting, that the Trustee should have discovered the fraud as claimed by the defendant not later than July 1, 1935 (Pre-trial Order, Tr. p. 55), the Chandler Act, if it be given a retroactive effect, would have on its effective date abrogated the right of the Trustee to bring this action, notwithstanding the fact that up to that moment the Trustee would have had until two years after the closing of the estate to do so. But we maintain that

the Chandler Act had no such retroactive effect. It acted prospectively only, save as to matters of procedure, and then only if the Court determines it is practical (See *Hastings v. H. M. Byllesby & Co.*, (N.Y.) 57 N.E. (2d) 737, 739-741, and *Pittman v. Bump*, 5 Ore. 17, 20. We refrain from quoting from or discussing these cases at this time, and likewise refrain from further arguing this phase. We so refrain because, first, we do not believe it will be necessary to determine this appeal on this point, and secondly, because the previous decisions by this Circuit Court of Appeals,<sup>1</sup> contrary to decisions in other circuits,<sup>2</sup> seem to indicate that, notwithstanding, the Bankruptcy Act prior to the Chandler Amendment be the applicable statute, still in a case like this, not based on preference, this Court would probably hold that the State Statute would still apply. We believe this Court has not gone so far, and that we could convince the Court that even under decisions in this circuit, Sec. 11(d) of the Bankruptcy Act prior to the Chandler Amendment would not bar this suit until two years after the closing of the estate. We do not waive the point, but we shall not further discuss it.

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<sup>1</sup>*Davis v. Willey*, 273 Fed. 397; *Meikle v. Drain*, 69 Fed. 2nd, 290.

<sup>2</sup>*Isaacs v. Neece*, 75 Fed. 2nd, 566; *Fuller v. Rock* (Ohio) 180 N.E. 367, 20 A.B.R. (N.S.) 655; *Sproul v. Gambone*, 34 Fed. Sup. 441, 443. In re *Handy Andy Stores* of L.A., 41 Fed. 2nd 98, 105; *Nairn v. McCarthy*, 120 Fed. 2nd, 910, 912.

## **II. (a) Action Brought Within Two Years of the Discovery.**

There is direct testimony to the effect that the discovery of the fraud occurred only within a month or two before the bringing of this action (Tr. p. 95, 96) and there is no testimony whatsoever of an earlier discovery.

## **II. (b) The Trustee Had No Information Charging Him With the Duty of Further Inquiry.**

We recognize the doctrine that where a party has the available means of discovery and is put on notice of such a character that it becomes his duty to make inquiry, then whether or not he makes such inquiry he is chargeable with the facts that such inquiry would ordinarily develop. We say we recognize this doctrine and its existence in ordinary cases, but we deny its impact in cases where the defrauding party has through secrecy and design made it hopeless for the fraud to be discovered. But this phase will be covered under a separate heading later. Accepting the doctrine, however, in its general aspect, it is maintained that the Trustee had no information of sufficient character to charge him with the duty of inquiry, nor any information which would have led him to believe that discovery would have followed inquiry. This statement is a legal conclusion from the evidence,



and of course such conclusion is as capable of being drawn by this Appellate Court as by the District Judge. What, then, was the information which came to the Trustee to charge him with a duty of further inquiry?

### **1. Newspaper Articles Not Such Information.**

The testimony at the most shows that the Trustee had the means available of obtaining information concerning certain suits brought by certain bondholders against the Western Bond and Mortgage Co. (Ex. 74 and 86) and by a bondholder against Farrington and others (Ex. 62). The means thus available to him was indicated by certain newspaper clippings included, among many documents, in a large credit file which credit file was introduced in the proceeding brought by the Trustee against the Bank of California (Ex. 162). These newspaper clippings refer to several suits, but in themselves made no reference to the charges which is the subject of this suit. The testimony is completely lacking to the effect that any of the plaintiffs in these several suits ever attempted to bring any information to the Trustee or to call to his attention any data concerning the frauds here alleged, or for that matter, any frauds. Was the Trustee, therefore, under such circumstances, chargeable with the duty to make inquiry, assuming for the nonce (which we deny) that the inquiry would have resulted in discovery. (Of this more later.) As was said by

this Court in the case of *Anglo California Bank v. Lazard*, 106 F. (2d) 693, 704:

“Appellants contend that the means of knowledge is the equivalent of knowledge. Appellees concede that appellees, or the owners, had the means of discovering the inadequacy of the selling price, but it is of no consequence that the facts disclosing fraud could have been discovered had an investigation been undertaken sooner. Appellees, or the owners, were not bound to make an investigation until they had knowledge of the facts of such a character as to put them upon a duty of inquiry.”

## 2. Existence of the Bankrupt's Books and Records.

The doctrine of the case of *Anglo California National Bank v. Lazard* also applies to the claim made by Farrington that the books and records of the bankrupt corporation were available and that discovery could have been made therefrom, notwithstanding his camouflaging of the books to prevent such a discovery.

It is perhaps true that had a thorough and complete examination been undertaken, at great cost, of the books and records of the Western Bond and Mortgage Co., the frauds may have been discovered, although that is somewhat of an assumption, for the books of other companies and individuals might have had to be scrutinized before such frauds could have been uncovered. But the question here is: was the Trustee under a duty to expend the estate's meager funds already committed for other purposes,

(viz., the carrying on of the Bank of California litigation), or to go in debt personally, or to expend moneys of his own in order to make an investigation, the results of which were uncertain? The Court must place itself, in making the conclusions, in the position the Trustee was in, at that time. The litigation against the Bank of California had begun and was being hotly contested by the Bank, who had adequate means to contest it. The Trustee who had accumulated from one to two thousand dollars in the estate (Exhibit 111—See Tabulation, p. 16 this Brief) realized that even if the case were won, an appeal would undoubtedly be taken, which might not stop at the Circuit Court of Appeals. The cost for transcribing testimony and records, for services of a certified public accountant, for travel in procuring testimony, for printing Transcript and briefs, would in all likelihood take all available funds, notwithstanding that this was a case in which the facts were pretty well suspected or discovered. We urge, with a feeling of sureness, that the Trustee was under no duty under the circumstances to indulge in any such extravagances, particularly since State accountants from the Attorney General's office had made an examination of the books and had reported to the Trustee (Tr. pp. 108-109, 192-193, 209-210), in which examination or report the frauds here at issue were not indicated (Tr. pp. 121-122, 209-210).

### **3. Revenue Agent's Report Concerning Additional Assessment of 1930 Taxes.**

It is also claimed by Farrington that the Trustee had the available means of discovery of his fraudulent acts in a revenue agent's report concerning the assessment of additional taxes for the year 1930. True, the Trustee knew that a report was in existence, although it had been removed from the records of the bankrupt (Tr. 146). The availability of such report to the Trustee through his ability to obtain a copy of it from the Department of Internal Revenue, it is claimed by Farrington, would have brought knowledge of the frauds here invoked. But we maintain with assurance that the fact that the Trustee may have known of the existence of a report containing recommendation for assessment of additional taxes for the year 1930 certainly did not charge him with the duty of obtaining this report where there was no intimation, inference or knowledge that such report contained any indications of fraud whatsoever.

Such reports of agents rarely indicate fraudulent transaction. Usually they contain the agent's interpretation of the regulations and the law as applied to the facts justifying a larger tax than returned by the taxpayer. They are usually concerned with matter of accounting. Why should the Trustee, we ask, have suspected that this report should have contained indications of fraud? Why should the Trustee expect the unusual?

We therefore maintain that the means in this connection of information available to the Trustee were not such as to charge him with the duty to seek out this report at that time.

## **II. (c) Would Inquiry, If Pursued, Have Resulted in Discovery.**

In only one instance of those just discussed is it even debatable that the Trustee owed a duty to investigate.

We have shown conclusively, we believe, that there was no such duty to initiate an extensive and costly examination of the books and records of the bankrupt, after a thorough examination by State auditors had been completed without results (Tr. p. 210), and after the Trustee, with some knowledge of bookkeeping, had gone over the books himself, also without results. We have also shown, we believe, with like conclusiveness, that no such duty existed, until need for it was indicated, to obtain a copy of the Revenue Agent's Report concerning 1930 taxes, for the Trustee had no intimation of the contents of such report, nor any reasonable cause to believe that such report would charge fraud (Tr. p. 120). When the duty arose to obtain such report in order to contest the tax claim of the Government based thereon the Trustee promptly obtained it (Tr. pp. 91-95, 120).

The only situation, therefore, open at all to de-



bate is the situation which arose when the newspaper clippings came to the attention of the Trustee in another connection and in other proceedings. Assuming therefore, for the sake of argument only, (while vehemently denying it) that the duty of inquiry arose upon the Trustee's awareness of the newspaper clippings contained in the Bank of California credit file, let us suppose therefore that investigation followed. Of course the only and obvious investigation indicated was of the court records of the cases referred to in the clippings. What would have been the reasonable result of such investigation? The Trustee would have discovered that there were three suits referred to in the clippings. Two of them were not against Farrington (Exhibits 74 and 77). The pleadings in neither of these cases even remotely referred to the frauds here alleged. Certainly after an inspection by the Trustee of such records, he neither would nor should have gone further. Therefore these two cases are out.

Now as to the other case, that of John Brockie v. Western Bond and Mortgage Company, C. H. Farrington et al, (Exhibit 62) instituted in the District Court of the United States for the District of Oregon in March, 1933: In that case had the Trustee gone to the records he would have discovered that the suit had been dismissed by John Brockie shortly after it had been brought (Exhibits 68 to 71) over the protest of Farrington, and at Brockie's cost (including a substantial special master's fee) which costs the Court



directed to be paid before dismissal. Irrespective of what the charges were in the complaint in that case, we are positive that we are justified in stating that the Trustee, as an ordinarily prudent man, would have ceased from further inquiry upon ascertaining the fact that the cause had been dismissed. Any normal person, however prudent, would be justified in immediately concluding that a suit dismissed at the motion of the party who brought it and at his cost over opposition of the defendants, was based on charges which to say the least were unfounded.

We maintain therefore that even were the Trustee under the duty to further investigate in this connection, such investigation would not have resulted in discovery of the frauds here assigned. Of course the Trustee is chargeable only with discovery of such facts as ordinarily would result from the investigation.

## **II. (d) Discovery, If Made, Would Have Related Only to First Claim.**

Let us continue further. Should this Court be of the opinion that the Trustee was under the duty to inquire and examine into the matters further in connection with the suits brought by others against the corporation and the suit brought against Farrington, what would the Trustee have discovered if such inquiry had been pursued? The suit or suits against

the corporation indicated in no way the frauds here charge. (See Exhibits 74 and 86). The Brockie suit against Farrington (Exhibit 62) indicated nothing whatsoever concerning the Consolidated Credit Corporation stock manipulation (the second claim). Consequently, inquiry induced by the newspaper articles, if followed through irrespective of reasonable cause to desist (the dismissal of the suit) could in no way have resulted in discovery of the fraud connected with the Consolidated Credit Corporation stock manipulations (the second claim).

Moverover, no inquiry whatsoever could have resulted in a discovery of the frauds charged in the second claim, in so far as the Revenue Agent' Report was concerned, for that report made no reference whatsoever of the Consolidated Credit Corporation stock manipulation. Thus, however soon or late the Trustee may have obtained the Agent's Report would not have affected discovery or failure to discover the frauds connected with that manipulation. It will be recalled that such frauds were discovered by the accountant upon probing for possible losses to offset asserted gains in connection with a contest of the Government's claim for taxes, which contest did not arise until 1943. Information concerning these frauds did not come from the Agent's Report.

We have heretofore covered the question of the Trustee's duty in regard to an exhaustive examination of the books of the bankrupt taken in considera-

tion the financial situation of the estate. We shall not do so again.

## II. (e) Balancing Trustee's Faults Against Farrington's Frauds.

We are not unmindful of the doctrine heretofore referred to that where there is means of information available, and there comes to one charged with the duty of inquiry relevant facts, a failure to pursue those facts charges him who has the duty to inquire, with the knowledge discoverable through such inquiry. In relation to statute of limitations, this doctrine is expressed in *Fleishhacker v. Blum*, (C.C.A. 9th) 109 F. (2d), 543, 548, as follows:

"The word 'discovery', as used in the statute, means actual knowledge, or knowledge of facts which, in the exercise of diligence, would have led to an actual discovery of the fraud."

The doctrine, however, is modified when the fraud alleged is of a secret nature and designedly covered up by the party charged. And so this Court, in the case of *Pickens v. Merriam*, 242 Fed. 363, 368, held that when fraud which is the foundation of a suit has been concealed, or is of such a character as to conceal itself, the statute does not begin to run until the fraud is discovered by the party suing.

But here there is a much wider principle involved. A Trustee, it is true, represents the creditors. He is elected by a majority of them who happen to be pres-

ent at the first meeting of creditors. After the Trustee's election creditors have no control of supervision over him. He does not report to them, and the creditors only official contact with him is through the Referee or the Court. They cannot command nor compel.

So with this in mind, what happens to creditors who have been defrauded by a officer of a bankrupt concern where the Trustee whom they can neither command nor compel fails to possess the sleuthing qualities which one with *post facto* wisdom may think a prudent man should possess? Assuming that a Trustee is ignorant or careless, or even reckless, or corrupt, should the fraudulent denuder of a corporation's assets profit at the expense of innocent creditors because of a trustee's failure to act or because of a trustee's reckless or even corrupt action? Should a trustee's negligence, carelessness or recklessness affecting innocent creditors, be weighed in the scales and be nicely balanced as against a defrauder, by whose cleverness a trustee may be lulled into carelessness? The answer suggests itself. Perhaps if a trustee were acting for himself or as the agent of another, who had complete control and supervision over him, his inaction or carelessness or negligence might result in the barring of an action against the defrauder. However, we pose the question whether under the circumstances here existing the creditors should be penalized by a meticulous balancing of faults between the trustee and the defrauder; the

balancing of carelessness or negligence, if there were such, as against secretive and camouflage fraud? We feel justified in urging the court not to permit such a doctrine to be established in this circuit.

### III. THERE WERE NO LACHES.

If the Trustee was under no duty to pursue inquiry, or if he was under such duty and the inquiry reasonably expected of him would not have resulted in discovery, or if, as lastly stated, his mere carelessness is not to be weighed against the fraud of the defendant, then this action is not barred. Assuming, therefore, that the Court will come to such conclusion, there is then no room for a discussion of laches. If the Court comes to a contrary conclusion, thus barring the action, then, of course, laches need not be discussed here.

In *Sedlak v. Sedlak*, 14 Or. 540, 541, Justice Lord said:

“The general rule, without doubt, is, that no lapse of time or delay in bringing suit will be a bar to the remedy in equity, provided the injured party, during the interval was ignorant of fraud. But the ignorance of such party must not have been negligent; for it, by reasonable diligence, the fraud could have been discovered, or ought to have been known, he will be deemed guilty of laches, or of acquiescence, and equity will refuse to interfere.”

In other words, if the action is barred laches becomes an academic question. If the action is not



barred the laches would not bar it under the facts in this case, and we feel no further discussion is necessary in that respect.

#### IV. COMMENTS ON DISTRICT JUDGE'S OPINION.

We are loath to be critical of so eminent and able a judge as Judge Fee, but the case at bar does not seem to have had his usual analytical attention. We feel, therefore, free to make some comments upon his opinion, and to point out what is believed to be his erroneous conclusions.

He praises, in one breath, the Trustee and his attorneys for their "years of unflagging zeal" to obtain a recovery in what he calls "the main chance" and then criticises them in the next breath for failing to pursue clues "that *might* have led to a like recovery" in this case. (Tr. p. 71).

He states in his opinion (Tr. p. 61):

"The newspapers carried accounts of the alleged civil and criminal liability of Farrington, some of which McBride had called to his attention, and there were *many suits* filed in court which contained positive allegations in relation thereto." (Emphasis ours.)

We assert, after careful scrutiny of the testimony in this case, that there is not one word of evidence therein that any suit except the suit of Brockie v. Farrington, et al, contained positive allegations in



relation to the civil and criminal liability of Farrington as to the frauds here charged. We have explained heretofore that the Brockie suit was dismissed at the motion of Brockie, and at his cost. Yet, Judge Fee does not remark on this phase.

Again, Judge Fee stated in his opinion that "In 1935, McBride knew of a tax claim asserted by the Internal Revenue Department". (Tr. p. 61). He then criticises McBride for not obtaining immediately a copy of the Revenue Agent's Report stating:

"Thus he procrastinated for all these years in obtaining the copy although from his experience in tax matters, he must have known that this document would have been invaluable in unwinding the tangled skein which he had in his hands." (Tr. p. 62).

It is difficult to understand the logic of these remarks. Judge Fee must know that the method of assessing additional taxes by the Government is through a recommendation or report of an agent. But the mere fact that such a report is made followed by an assessment of additional tax in no way indicates that a charge of fraud is asserted. Not one case in a thousand of additional assessment cases arises through fraud. Usually it is because someone has omitted a profit made, or has improperly charged off a loss, or because a loss is taken in one year when it should have been taken in another, or because the tax payer felt he had an exemption when he did not. There are a thousand and one other reasons for addi-

tional assessments, and all additional assessments are based on recommendation of an agent contained in a report. Why, therefore, should Judge Fee surmise that McBride should be charged with a suspicion that the tax claim was based upon a report of an agent indicating fraud? There really can be no criticism of McBride for not obtaining a copy of the Agent's Report earlier than he did, and the animadversions of Judge Fee in this connection, we think, are unjustified.

As outlined in our Brief, this report was attempted to be obtained by McBride shortly after the Government filed a claim for taxes. McBride explained that when he went to the Referee and stated his intentions to file objections to the Government's claim the Referee with obvious propriety indicated that it would be unnecessary to file such claim until there was money in the estate on which the Government could realize in the event the claim was allowed. In other words, on the Referee's direction he took the practical means of postponing the filing of objections to the tax claim until there was money in the estate on which the Government could realize in the event the claim was allowed. Not until moneys came into the hands of the Court in a sufficient amount to pay all or a substantial part of the tax claim did there arise the occasion to contest the Government's claim. As soon as it arose the Trustee obtained the agent's report on which the tax was based. But Judge Fee

never comments on this phase of the matter in his opinion of some twelve printed pages.

Now again in connection with McBride's failure to obtain the Revenue Agent's report Judge Fee states, censoriously:

"After he knew an income tax report existed, McBride called at the office of the agent of Internal Revenue but found no record there. Some time after this he found that Robert Jacob, an attorney, had a copy of this document. For three or four years after he had this knowledge he made no effort to see the report. Finally, he called at Jacob's office. He found that Jacob was out of the office and immediately abandoned all further effort." (Tr. p. 61, 62).

Now Mr. McBride testified as follows (Tr. p. 120) :

"Q. Then, as I understand you, the extent of your efforts to ascertain the basis of this claim of the Government for \$50,000 was one visit to the office of the Internal Revenue Department in Portland and one visit to Bob Jacob's office, on which occasion you found him to be out of town?

A. Yes. I do not remember any other times that I went after that. It was not coming up at that particular time, and the assessment that was made explained it enough to know how much they claimed, and there did not seem any necessity for going into it so much deeper until the claim was acted on before the Referee, so I did not go any further with it when I found that Mr.

Jacobs was not there, and I did not know he even had it.”

Again, Judge Fee states (Tr. p. 67) :

“All the records of the bankrupt were placed in the Trustee’s hands and he had some assistance and *sufficient money* to make an investigation of them.”

Now the evidence introduced by the defendant shows (Ex. 111) that at no time prior to February 11, 1943, when the first monies were received from the Bank of California judgment, did the Trustee ever have more than \$2400 at any time, and the testimony further shows that the accountant’s bill for services in connection with the Bank of California matter alone was \$2500. (Tr. 110). How, then, could Judge Fee find that the estate have sufficient monies on hand to make the investigations necessary?

We need continue no further.

## CONCLUSION

We firmly maintain that the District Court’s judgment of dismissal should be reversed, since it held erroneously that the suit at bar was barred at any time previous to two years after the closing of the estate.

But if the Court were correct in that holding, we urge that it was certainly in error in holding that the Trustee was barred in his action based on the fraudu-

lent manipulations of the Consolidated Credit Company stock, since no intimation came to the Trustee of any nature in connection with that fraud.

Moreover, it is as firmly maintained that the Trustee's action was not barred by reason of any inactivity or failure to act in connection with the fraudulent appropriation of the Guaranty Company's stock, and that, therefore, the Court erred in holding to the contrary.

And it is further asserted that the Trustee's suit was not barred when there is taken into consideration the Trustee's lack of action (if any fault could be ascribed to him for such inaction) as against the appellee's fraudulent actions and manipulations. For failure to so distinguish, we urge, the Court was in error, and for this reason also, the judgment of dismissal should be reversed.

Respectfully submitted,

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In the United States  
**Circuit Court of Appeals**  
For the Ninth Circuit

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,  
*Appellant,*

vs.

C. H. FARRINGTON,  
*Appellee.*

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**BRIEF OF APPELLEE**

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Upon Appeal from the District Court of the United  
States for the District of Oregon.

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In the United States  
**Circuit Court of Appeals**  
For the Ninth Circuit

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,  
*Appellant,*

vs.

C. H. FARRINGTON,  
*Appellee.*

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**BRIEF OF APPELLEE**

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Upon Appeal from the District Court of the United  
States for the District of Oregon.

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**ABSTRACT OF THE CASE**

Plaintiff is Trustee in Bankruptcy of Western Bond & Mortgage Company, a corporation, hereinafter referred to as Western Bond and defendant was in 1929 and 1930 a stockholder, director and president of the corporation.

October 2, 1943, plaintiff as Trustee in Bankruptcy, commenced this suit in equity to recover from defendant the value of property alleged to have been fraudulently obtained by defendant from the corporation. The complaint charges two fraudulent transfers. One transfer is alleged to have been made on **December 12, 1929**, involving 40,000 shares of the capital stock of Consolidated Credit Corporation, which stock was owned by the Western Bond. The other is alleged to have been made on **December 20, 1930**, involving the transfer of the capital stock of Western Guaranty Company which was owned by Western Bond.

It is alleged that the transfers were a fraud on creditors and that (Tr. p. 2):

“The action arises under Section 67 and Section 70 of the United States Bankruptcy Act . . . .”

November 25, 1931, a Petition in Bankruptcy was filed against the Western Bond. (Tr. p. 27).

August 13, 1934, plaintiff was appointed Receiver in the bankruptcy proceeding. (Tr. p. 27).

December 4, 1934, plaintiff was appointed Trustee. (Tr. p. 27).

To avoid the bar of the Statute of Limitations and Laches plaintiff alleged that he did not discover the fraud until 1943. (Tr. p. 7).

After issue was joined, the court below made an order segregating the issues of limitations and laches from the issues on the merits and directed that they be first tried and determined. (Tr. p. 7).

The suit was tried on the issues of limitations and laches. Judge Fee rendered a written decision in favor of defendant (Tr. pp. 60 to 72) in which he held **upon the facts** and upon the law (a) that the case was governed by the Oregon Statute of Limitations which fixes a period of two years from the discovery of fraud for the commencement of an action; (b) that plaintiff could have discovered the alleged fraud by the exercise of reasonable diligence more than two years prior to the commencement of the suit and was therefore barred by the Oregon Statute of Limitation and (c) that the long delay in challenging the transactions resulted in prejudice to defendant because in the interim participants in the challenged transactions and witnesses having knowledge of material facts had died, that defendant **"had been robbed of a means of defense"** (Tr. p. 71), and that plaintiff was guilty of laches which barred recovery.

The opinion was handed down after an extended colloquy between Judge Fee and counsel for plaintiff-appellant (Tr. p. 278 to 303) in which the court sought to have plaintiff clarify his theory of the case.

The court then made Findings of Fact and Conclusions of Law upon the issues of limitations and laches (Tr. p. 72 to 74).

With respect to discovery of the fraud, the Findings of Fact recite (Tr. p. 73),

"Plaintiff was appointed trustee in bankruptcy of Western Bond and Mortgage Co. on

December 12, 1934, and all of the records of said corporation were promptly placed in his hands, including a litigation record pointing to the transactions on which plaintiff bases his claims against defendant.

“Prior to 1936 plaintiff had actual knowledge or was in possession of information which was sufficient to guide him to actual knowledge of the matters alleged in the complaint.

“Plaintiff failed to pursue with reasonable diligence the information which had come into his possession prior to 1936 and which pointed to the transactions referred to in the complaint.”

With respect to laches, the Findings of Fact set forth (Tr. p. 74),

“Prior to the bringing of this action participants in the transactions referred to in the complaint and others who had known the material facts had died and defendant was deprived of a means of defense through their evidence.”

**This Finding of Fact is not challenged by any proper specification of error.**

The Conclusions of Law recite that the action is barred by the provisions of the Oregon Statute of Limitations; that the action is barred by plaintiff's laches and that defendant is entitled to judgment of dismissal (Tr. p. 74).

On the said Findings of Fact and Conclusions of Law judgment dismissing the complaint was entered, and plaintiff now appeals from said judgment.

## THE QUESTIONS INVOLVED

1. Are the specifications of error (applt's. br. p. 18) sufficient to present any question for consideration of this court?
2. **Re: Laches**—Is there any substantial evidence to support the findings of the fact?
3. **Re: Statute of Limitations**—(a) Is the Oregon Statute of Limitations applicable? (b) Is there any substantial evidence to support the findings of fact?
4. Are the conclusions of law warranted by the findings of fact?

## PRELIMINARY STATEMENT

Appellant presents this case as though the issues for determination arise upon a demurrer to the complaint. He adopts the allegations of the complaint and assumes them to be true. The appeal is not from a judgment entered upon an order sustaining a demurrer to the complaint.

The appeal is from a judgment **entered upon findings of fact** and conclusions of law made **after a trial of the issues of fact** and law on the questions of **laches and limitations**.

While the court below did not try and determine the issue as to the alleged fraudulent transfers, and this Court is not now called upon to determine that issue, it cannot be assumed in this case that the allega-



tions of the complaint charging the defendant with the fraudulent transfers are true, as in the case of a judgment based upon a demurrer to a complaint. In this case issue was joined as to these allegations. They have not been tried or determined in this case. Neither has there been any adjudication in any other proceeding that Farrington was responsible for any fraudulent transfers. Hence the assumption of fraudulent conduct by Farrington in this case is unwarranted, and should not prejudice the court in considering the **only issues** which were determined and are now before the court, to-wit: laches and limitations.

Although charges of fraud have been hurled against this defendant since <sup>1931</sup> there has never been any adjudication of misconduct on defendant's part in any proceeding and none in the case at bar.

We, therefore, challenge appellant's right to present his case in this court upon the **assumed guilt** of the defendant, contrary to the cardinal rule that **fraud is never presumed**.



**I**

**THE SPECIFICATION OF ERRORS ARE INSUFFICIENT TO PRESENT ANY QUESTION FOR REVIEW UPON THE ISSUE OF LACHES**

Rule 20(d) of this Court requires that the Specification of Errors,

“Shall set out separately and particularly each error intended to be urged.”

**And when Findings of Fact are made,**

“The specification shall state as particularly as may be wherein the Findings of Fact and Conclusions of Law are alleged to be erroneous.”

Findings of Fact on the issue of laches were made in this case.

The Specification of Errors directed to this issue in appellant's brief is as follows: (P. 19)

“The Court erred in holding that the Trustee was guilty of laches.”

We submit that the specification is not a compliance with Rule 20(d), as construed by this Court because it does not point out whether,

- (a) Appellant intends to challenge the admission or rejection of evidence pertaining to this issue,
- (b) Intends to challenge the credibility of the witnesses,

- (c) Intends to challenge the sufficiency of the evidence to support the Findings of Fact,
- (d) Intends to challenge the sufficiency of the Findings of Fact to support the conclusions of law that the suit is barred by laches.

Appellant's specification "lumps the entire case", and throws it into the lap of the court.

**In American Surety Co. v. Fischer Warehouse Co., 88 Fed. (2d) 536-539 (9th Cir.) (1937),** this Court said:

"It is not sufficient that appellant assert generally that the trial court made wrong findings and reached wrong conclusions and then and thereby **invite this court to retry the cause** without indicating to us in such assignments in what respect or for what reason the findings or conclusions are claimed to be in error."

In considering the sufficiency of the assignment of errors in that case, this Court propounded the following inquiry:

"What was the erroneous basis used, or the erroneous step made by the court which shows his conclusion was wrong? The court might have erred in reaching his conclusion by considering testimony erroneously admitted; by erroneously excluding evidence; by finding a fact not supported by substantial evidence; by the erroneous application of law; or by some other erroneous action. But we consider alleged errors, and if none are assigned, there are none to consider."

**In United States v. Bollman, 81 Fed. (2d) 1009, 9th Cir.,** the Court below made Findings of Fact on which the judgment appealed from was entered. The Court

held that where "findings are not complained of" all errors "based on the trial court's findings are therefore decreed abandoned."

In *Krause v. Snyder*, 87 Fed. (2d) 723-725 (8th Cir.) (1937), the court held:

"The party complaining of the action of the lower court **'must lay his finger upon the point of objection** and must stand or fall upon the case he made in the court below'."

In *Cohen v. United States*, 142 Fed. (2d) 861, 8th Cir. (1944), the Court held:

"(1) As has been observed, the action was tried to the court without a jury. No questions are raised as to the admissibility of evidence, nor is there any specific challenge to any ruling of the court, **nor are the findings of the court challenged as not being sustained by the evidence.** . . . . .

"In *E. R. Squibb v. Mallinckrodt Chemical Works*, Judge Stone, speaking for this court . . . said (69 F. (2d) 687):

' . . . . In short, the appellant has **lumped into this assignment the entire case**, except objections to evidence and no such objections are urged here or preserved in any assignment. All that this assignment amounts to is that a wrong decree was entered. It is a clear violation of rule 11 requiring that assignment of errors shall 'set out separately and particularly each error asserted and intended to be urged' . . . .

" 'Since the specifications and assignments of error present nothing for our consideration, the decree must be and is affirmed.' "

‘In the instant case the questions propounded in the brief challenge no particular action or ruling of the court but at most **question ‘the entire case.’** If they be construed as an attempt to question the court’s findings as not being sustained by the evidence, it is clear that they do not point out where in or in what particular the evidence is lacking to sustain the findings.”

In the case at bar, appellant has “lumped” into the specification the “entire case”, insofar as it relates to the issue of laches. The court is invited “to retry the cause” without indicating in what respect the court erred and without challenging the findings of fact.

Under the foregoing decisions the specification of errors with respect to the issue of laches, is insufficient to raise any question for determination by this court. The decision of the court below on this issue should therefore be affirmed.

If appellee is correct in this contention the judgment appealed from must be affirmed because the remaining issue as to the application of the statute of limitations then becomes academic.

## II

## SCOPE OF REVIEW IN THIS COURT

The issues of laches and limitations were **tried upon the facts**. Findings of Fact and Conclusions of Law were made thereon adverse to the allegations of the complaint.

**Rule 52 of the Rules of Civil Procedure** provides that:

**"Findings of Fact shall not be set aside unless clearly erroneous."**

It is the established rule of this Court, as it is in all of the circuits, that a finding is not **"clearly erroneous"** if there is **"any substantial evidence"** to sustain it.

Assuming without admitting that the Specification of Errors properly present the issues, the scope of review in this Court is limited to the ascertainment of the existence of **"any substantial evidence"** to support the Findings of Fact. It is not even suggested anywhere in the specifications that the Conclusions of Law are not supported by the Findings of Fact.

In **Rogers v. Union Pacific R.R. Co.**, 145 Fed. (2d) 119, (9th Cir.), this court said that when a Finding of Fact is supported by substantial evidence, **"we must accept it as correct."**

In **Lumbermens Mutual Casualty Co. v. McIver**, 110 Fed. (2d) 323 (9th Cir.) 1940, this court adopted the rule announced by the Supreme Court of the United States in **State Farm Insurance Co. v. Coughran**, 303 U. S., 485-58, Sup. Ct. 670, as follows:



“Under applicable statutes and repeated rulings here, the matter open for consideration upon the appeal was whether the findings of the trial court supported its judgment. **To review the evidence was beyond the competency of the Court.**” (citing authority.)

**In Gaytime Frock Co. v. Liberty Mutual Insurance Co., 148 Fed. (2d) 694, 7th Cir., 1945, the court held:**

“Moreover, it is clear from what we have said that the sole question here involved, revolves about the propriety of the **inferences and conclusions drawn from the evidence by the trial judge, who had the primary function of finding the facts and choosing from among conflicting factual inferences those which he considered most reasonable.** Under such circumstance our power is limited to a determination of whether those inferences and conclusions have any substantial basis in the evidence. If such a basis is present the process of judicial review is at an end, . . . . . And even where there is no dispute about the facts, if different reasonable inferences may fairly be drawn from the evidence, we are forbidden to disturb the findings based on such inferences unless they are clearly erroneous.”

**In Scroggs v. American Stove Co., 142 Fed. (2d) 297, 7th Cir. 1944, the court held:**

“Our function is limited to ascertaining if there is **any** such evidence, and in doing so we **must consider the record in the light most favorable to the plaintiff.**”

(All emphasis in quotations supplied by counsel for appellee.)

It must be remembered in this case that the plaintiff had the burden of proof upon the two issues here



involved. The issues were decided against the plaintiff, and so in this case, in order to establish error, he must demonstrate that there is no substantial evidence to support the Findings of Fact, and that he has himself sustained his case by preponderance of the evidence.

**Columbian National Life Insurance Co. v. Goldberg, 138 Fed. (2d), 192, (6 Cir.).**

We submit that an examination of the record will disclose not only **some** substantial evidence to support the findings of fact, but that no other conclusion was possible.

## III

**APPELLANT'S CAUSE OF SUIT IS BARRED  
BY LACHES. THE FINDING OF FACT IS  
SUPPORTED BY SUBSTANTIAL EVIDENCE.**

## SUMMARY

## I.

Appellant's brief in dealing with the subject of laches (p. 35-36) does not assert or attempt to demonstrate that there is no substantial evidence to support the findings of fact.

## II.

Appellant's contention that if the cause of action is not barred by the statute of limitations, it would not be barred by laches, is erroneous as a matter of law.

## III.

The application of the doctrine of laches does not merely depend upon the reasons for plaintiff's delay. The doctrine of laches concerns itself with the effect of the delay upon the ability of the defendant to defend himself against the charges and whether he was adversely affected by reason of changed conditions.

## IV.

The death of participants in and witnesses to the transaction out of which the litigation arises, the loss of evidence, the dulling of the memory of the surviving parties or witnesses which subject defendant to the hazard that he may not be able to adequately present his defense, makes applicable the doctrine of laches.

## V.

The record establishes and the court below made findings of fact that the defendant **would be prejudiced** in this case in the presentation of his defense by reason of the loss of evidence from the death of participants and witnesses. This finding is not challenged.

## VI.

Appellant was guilty of gross negligence and failed to exercise reasonable diligence in asserting the claims.

## ARGUMENT

It is highly significant that appellant does not in his brief make the slightest attempt to demonstrate that the court below committed error in making the finding of fact that defendant was prejudiced by the delay due to the loss of witnesses through death.

The sole contention on the subject of laches is embraced in appellant's statement (br. p. 35):

"If the action is barred, laches become an academic question. If the action is not barred laches do not bar it . . . ."

The first sentence is obviously true. If the action is barred by the statute of limitations it is a complete defense and it is immaterial whether the action is also barred by laches.

But the second sentence which involves the converse is not true. It is settled beyond question that the doctrine of laches applies even though the action is not barred by the statute of limitations.

In 19 Am. Jur. 345, the text says:

"On the other hand, where an equitable remedy is sought, the court may refuse its aid although the period which has elapsed without suit is less than that which is prescribed by the statute."

In *Wilson v. Wilson*, 41 Ore. 459-463, the Supreme Court of Oregon held that the laches will bar relief

**"although the full time may not have elapsed which would be required to bar a remedy at law."**

In *Sedlak v. Sedlak*, 14 Ore. 540, the only case cited by appellant, the Oregon Supreme Court in considering the application of the doctrine of laches said:

**"Sometimes the analogy of the statute of limitations is implied; sometimes a longer period than that prescribed by the statute is required; in some cases a shorter period is sufficient."**

The decisions of the Supreme Court of the United States, are to the same effect.

*Alsop v. Riker*, 155 U.S. 448-15 Sup. Ct. 162.

*Whitney v. Fox*, 166 U.S. 637-17, Sup. Ct. 713.

*Patterson v. Hewitt*, 195 U.S. 309-25, Sup. Ct. 35.

(All empsasis in quotations supplied.)

The court below decided the question of laches upon the facts. It made the specific finding of fact that:

**"Prior to the bringing of this action, participants in the transactions referred to in the complaint and others who had known the material facts, had died, and defendant was deprived of his means of defense through the evidence." (Tr. p. 74).**

In his opinion, Judge Fee pointed out (Tr. p. 70-71) that the transactions were consumated in 1929, ap-

proximately fifteen years ago; that the petition in bankruptcy was filed in 1931; that extensive investigations were made at that time; that the **main actors in the transaction**, with the exception of defendant, **are now dead**, as well as others who have known material facts and that there is “a detriment to the defendant in that he has been robbed of his means of defense by the death of witnesses and participants.” The suit was commenced in 1943 (Tr. p. 12).

The specification of errors does not challenge this finding of fact, nor is it argued in the brief that there is no substantial evidence to support this finding of fact.

It has been held that “**laches is a question of fact**”, and that “an appellate court will not interfere with its (trial court) discretion in this respect, unless manifest injustice has been done, or unless its conclusion cannot reasonably be held to find support in the evidence.”

**Wolpert v. Gripton, 2 Pac. 2d, 767 Cal.**

Before demonstrating that there is substantial evidence to support the finding of fact, we call attention to the cardinal principles that govern the application of the doctrine of laches.

In **Wood v. Davin, 122 Ore. 74-81**, the Oregon Supreme Court adopted the principles enunciated by the Supreme Court of the United States in **Hammond v. Hopkins, 143 U.S. 283**, in which Chief Justice Fuller said:

“No rule of law is better settled than that a court of equity will not aid a party whose applica-



tion is destitute of conscience, good faith and reasonable diligence, but will **discourage stale demands** for the peace of society by refusing to interfere where there has been gross laches in prosecuting rights, or where long acquiescence in the assertion of adverse rights has occurred. The rule is particularly applicable where the **difficulty of doing entire justice** arises through the death of the principal participants in the transaction complained of, or of the witness or witnesses, or by reason of the original transactions having become so obscured by time as to render the ascertainment of the exact facts impossible."

In *Wilson v. Wilson*, 41 Ore. 459-463, the Oregon Supreme Court held:

"If by the laches and delay of the complainant it has become **doubtful** whether adverse parties can command the evidence necessary to a fair presentation of the case on their part, . . . . . a court of equity will not interfere to give relief, but will remain passive."

In *Penn. Mutual Life Insurance Co. v. Austin*, 168 U.S. 685, the Supreme Court said:

"It is well established that if by laches and delay of the complainant, it has **become doubtful whether adverse parties can command the evidence necessary** to a fair presentation of the case on their part, as for instance, **where parties interested and witnesses have died in the interim**, . . . . . a court of equity will not interfere to give relief but will remain passive."

In 21 C.J. 226, Sec. 222, the writer says:

"**Evidentiary Effect of Delay.** Long lapse of time, if unexplained, may create or justify . . . . . a presumption that the evidence



of the transaction in issue has been lost or become obscured, or that conditions have changed since the right accrued, and that in consequence the adverse party, would be prejudiced by its enforcement."

In 21 C.J. 236, the writer says:

"To bring the rule into operation, it is not necessary that the court should be convinced that the original claim was unjust or has been satisfied; it is sufficient if the court believes that under the circumstances it is too late to ascertain the merits of the controversy. . . . In any event, loss or obscuration of evidence is a material circumstance to be considered in determining whether the asserted claim shall be enforced; it creates or justifies a presumption against the existence or the validity of plaintiff's right and in favor of the adverse right of defendant."

**In Sheehan v. Municipal Light & Power Company,** 54 Fed. Supp. 169-173, affirmed 151 Fed. 2nd 65, the court held:

"The testimony of Leach and Lasher and of officers of Edison Company, its general counsel, its attorney and many others who participated in the transactions who are now dead, is now unavailable. Minnie Sheehan accordingly was guilty of laches prejudicial to the defendants." (citing many cases.)

We submit that in the case at bar there is ample evidence to support the findings of fact of the court below on the question of laches, and that the facts found by the court below brings the case within the principles set forth in the foregoing authorities.

To fully appreciate the effect of the 15-year delay it is necessary to briefly outline the nature of the transactions out of which this suit arises. The two challenged transactions took place in 1929 and 1930, respectively. The suit commenced in 1943 and tried in 1944.

The essence of the charge with respect to the 1930 transaction is that defendant-appellee entered into a scheme with one Edward F. O'Flynn, who was president and in control of a corporation called the Massachusetts Mortgage Company, by which defendant caused the Western Bond and Mortgage Company to transfer to him or corporations controlled by him, assets owned by the bankrupt corporation, to-wit, a block of Western Guaranty Stock valued in excess of \$300,000 in exchange for certain assets which defendant simultaneously was to receive from O'Flynn, or the Massachusetts Mortgage Company, which had no value. The alleged valueless assets are as follows:

- (a) 100 shares of capital stock of Lake Lucerne Co.
- (b) Conditional Sales Contracts of automobiles.
- (c) Chattel mortgage on personal property.
- (d) Promissory note made by Birwell and indorsed by Massachusetts Mortgage Co.
- (e) Note of Massachusetts Mortgage Co.

The alleged vice in the transaction is summed up by plaintiff's witness, Erickson, to<sup>be</sup> the worthlessness of the assets received by Western Bond as considera-

tion for the transfer of the Western Guaranty stock (Tr. p. 160-164).

Edward F. O'Flynn, who was the principle participant, in the transaction, died long prior to the commencement of this suit (Tr. p. 137).

The defendant was represented in that transaction by Arthur C. Spencer, an attorney. He died prior to the commencement of this suit (Tr. p. 197).

Judge Carey was Corporation Commissioner of the State of Oregon. Investigation into the affairs of the bankrupt corporation, including the transfer of its assets, were carried on by authority of his department. He died long prior to the commencement of this suit (Tr. p. 198).

Plaintiff claims that he was prevented from carrying on investigation by Hon. A. M. Cannon, referee in bankruptcy, in charge of the bankrupt estate on the alleged ground that it did not seem likely that the estate would have assets (Tr. p. 91-92). The referee in bankruptcy died long before the commencement of this suit and was not available to admit or deny the plaintiff's excuse for the failure to carry on the investigation.

All persons participating in the transfers by and to the bankrupt corporation, are charged with bad faith, with causing misleading and false entries to be made in the books and that the transactions were hidden and disguised by the organization of dummy corporations (Tr. p. 7).

In order to determine the charges thus made, the good faith of the transactions, the honesty of purpose, the regularity of the transactions, the reasons which motivated the transactions and the purposes sought to be obtained, it would be necessary to bring before the court the actors who participated in the transactions and the witnesses who had opportunity to observe and know what was taking place. It would be necessary to establish the entire background and setting in which the transactions took place.

It is obvious that the death of Edward F. O'Flynn and of Mr. Arthur E. Spencer precludes any fair presentation of the history and the facts pertaining to the transaction. They were the principal participants therein. They alone could bring before the court all those details from which the court could determine the good faith of the transaction.

The death of the referee in bankruptcy made it impossible to challenge the truth of the trustee's testimony by which he attempts to throw the blame for his inaction upon the referee in bankruptcy. We believe that if the referee in bankruptcy was alive he would have denied the story that he discouraged investigation of the matters under consideration. But he is not here and defendant is deprived of the opportunity to test the truth of that story. It is not likely that the Referee would sanction failure to perform the mandatory duties imposed on the trustee by **Sec. 47a-7 and 8 of the Bankruptcy Act.**

The record discloses that difficulties were encountered from the loss of records and efforts to locate them were fruitless.

It is obvious too that the defendant would be at a tremendous disadvantage and subject to a great hazard in any attempt to disprove the allegation that the assets received by the bankrupt corporation were without value.

Fifteen years after the transaction we would be called upon to investigate the financial condition of the Lake Lucerne Company to ascertain the book value or intrinsic value or market value of 100 shares of its capital stock. This would involve the ascertaining (as of 1929-1930) of all of the assets and liabilities of that corporation, the value of its assets, the nature of its business, whether its operations were profitable, and a multitude of elements and details which are necessarily involved in determining the value of the capital stock of a corporation **which is not listed on a stock exchange.**

Fifteen years after the transaction we would be called upon to investigate the value of a block of automobile conditional sales contracts. This would involve an intimate knowledge (as of 1929-1930) of the particular automobiles, the makes, the age, the physical condition, the relation between the value of each automobile and the balance owing thereon, the financial responsibility of the purchaser and a multitude of other facts which is inherent in any inquiry as to the value of any conditional sales contracts, including expert testimony as to the market value of the auto-



mobiles themselves **as of that time.**

Fifteen years after the transaction we would be called upon to investigate the value of the chattel mortgage upon the personal property. This would, of course, require evidence of the kind and character of the personal property, its physical condition, the market value of the property at that time, as well as investigation as to the responsibility of the maker of the note and mortgage at the time of transfer.

Fifteen years after the transaction we would be called upon to investigate and determine the value of the Birwell note, which was indorsed by the Massachusetts Mortgage Company. This would involve an investigation of the financial responsibility of the maker of the note, knowledge of his assets and liabilities as of that time and the investigation into the financial responsibility of the Massachusetts Mortgage Company, the indorser on said note which would, of course, involve investigation of the assets and liabilities of that company and the multitude of details which is inherently involved in such an investigation.

We believe that the court could take judicial notice of the difficulties which would now present themselves in a trial of the issues of the value of those assets at that time. It is obvious that defendant would be greatly prejudiced if **now** called upon to meet that issue.

The burden was on the plaintiff to plead and prove facts which would prevent the bar of laches



from applying to this case. Plaintiff recognized and assumed that burden. To that end he made allegations in his complaint to excuse laches and introduce evidence for the purpose. It was incumbent upon plaintiff to show affirmatively by clear and convincing evidence that the defendant would not be prejudiced by the delay. This he could only do by the introduction of evidence that the means by which all of these questions could be fairly tried and justly determined, were available. Instead, plaintiff's own case demonstrated the inability to produce important evidence, important witnesses, lack of essential records, and the dullness of memory of those who purported to give some information upon that matter involved.

It is not only "doubtful" whether defendant can command the evidence necessary to a fair presentation of the case on his part, (**Penn. Mutual Life Case**, 168 U.S. 687), but it is well nigh impossible to do so. As it was said in **Smith v. Thompson**, 54 Am. Dec. 126-129 Va.:

"There can no longer be a safe determination of the controversy and their (plaintiff's) adversaries are exposed to the danger of injustice from the loss of information and evidence."

Under similar circumstances the court in **Hawley v. Von Lanken**, 106 N.W. 436, said:

"Any conclusion the court may arrive at must at best be conjectural. . . . ."

It is not necessary in order for the bar of laches to be applied that it should appear to a certainty

that the defendant would be prejudiced by the lapse of time. It is sufficient if it is "doubtful" whether he can fairly present his defense and that it is "too late" to ascertain the merits of the controversy. (21 C.J. 236.)

The 1929 transaction involved the transfer of 40,000 shares of capital stock of Consolidated Credit Corporation, which was owned by the Western Bond and Mortgage Company, in exchange for all of the capital stock of the Keystone Finance Company (Tr. p. 6). The vice claimed in that transaction is that the Western Bond was already the "beneficial owner" of the Keystone Stock and therefore, received nothing of value for the transfer of the Consolidated stock.

Plaintiff attempted to develop the "beneficial ownership" of the Keystone stock through a rather involved process.

Erickson, the accountant, testified (Tr. p. 148) that he found from the minute book of the Keystone Company that the stock of that company when organized was paid for by the transfer to it of 8920 acres of land, which was known as the Keystone Ranch. This conveyance to the Keystone Company in payment of the original subscription to its stock was made by two individuals, Tapfer and Snodgrass (Tr. p. 169). The witness, Erickson, pointed out, however, that in 1925, that ranch stood in the name of Russell Land and Livestock Company, which was a wholly owned subsidiary of Western Bond (Tr. p. 148) and it is therefore asserted that the parties who purported to convey the ranch to the Keystone Corp. for

its stock, had no title, that the title was actually in the Russell Land and Livestock Company since 1925, which was a subsidiary of the Western Bond, and therefore, Western Bond was the owner of the ranch through the medium of the Russell Land and Livestock Company.

Erickson testified that the abstract of title showed that **prior to 1925** the ranch was owned by a man named Russell, that he transferred it to the corporation, Russell Land and Livestock Company **in 1925** and **in 1929**, Russell Land and Livestock Company, transferred the property to the Keystone Finance Company, but Tapfer and Snodgrass are not shown as being at any time as owners of the land (Tr. p. 169). This is the trustee's contention with respect to that item.

Now, it is apparent that the determination of that issue depends upon whether Tapfer and Snodgrass were the legal or equitable owners of the ranch, or Russell Land and Livestock Company was the owner.

It must be remembered that Erickson only testified to what an abstract of title purported to show. But this does not preclude the fact that Tapfer and Snodgrass may have been the legal or equitable owners of the ranch at the time it was conveyed to the Keystone Finance Company. It may be that it was bought with their money and that they had the equitable estate. An abstract of title does not determine ownership. It merely purports to show what the records of a county clerk's office discloses. But all titles are not determined by recorded instru-

ments. Frequently they depend upon inheritance, through descent, and distribution or by will. They may be evidenced by unrecorded conveyances which are valid as between the immediate parties and other facts which give rise to equitable estates.

To compel defendant to try the issue of **title in Tapfer and Snodgrass** subjects him to the type of hazards recognized by the authorities which we have cited. There is **no evidence whether Tapfer and Snodgrass were available** so that the facts pertaining to their interest in the land could be ascertained. In view of the fact that plaintiff has the burden of proof, it was incumbent upon him to show that Tapfer and Snodgrass were available and the means by which the true ownership of that title, **legal as well as equitable**, can not be determined with the degree of certainty which a judicial determination contemplates.

The difficulty in meeting that issue, due to the lapse of time, warrants the application of the bar of laches.

### **Re: Lack of Diligence**

Appellant presents the question of laches as though it were conceded or the court had found as a fact that appellant had exercised reasonable diligence in ascertaining the facts, and in the commencement of the suit. He cites the **Sedlak case** (appellant's brief, p. 35), which recognizes the rule that lapse of time will not bar a remedy if the plaintiff was ignorant of the fraud. But the very excerpt which the

appellant cites says that ignorance **must not be due to negligence** and that

“if by reasonable diligence the fraud could have been discovered or ought to have been known, he will be deemed guilty of laches or acquiescence and equity will refuse to interfere.”

**In the case at bar, the court made findings of fact contrary to the assumed fact upon which appellant proceeds.**

The findings set forth (Tr. p. 73):

“Prior to 1936 plaintiff had actual knowledge or was in possession of information which was sufficient to guide him to actual knowledge of the matters alleged in the complaint.

**“Plaintiff failed to pursue with reasonable diligence the information which had come into his possession prior to 1936 and which pointed to the transactions referred to in the complaint.”**

The very foundation for appellant's contention is thereby removed and he is brought within the rule which precludes relief to the plaintiff.

The only way appellant could escape the effect of these findings is to demonstrate that there is not “any substantial evidence” to sustain those findings and that they are “clearly erroneous”, and that, appellant has not done.



## IV

**THE OREGON STATUTE OF LIMITATIONS APPLIES TO THE CASE AT BAR. IT IS NOT GOVERNED BY SECTION 11(d) OF THE BANKRUPTCY ACT (11 U.S.C.A., 29(d) ), BECAUSE THE CAUSE OF ACTION PROSECUTED BY THE TRUSTEE IS AN INHERITED ONE.**

## ARGUMENT

The court below held that the cause of action set forth in the Complaint was not created by the Bankruptcy Act; that the cause of action was in existence prior to and independent of the bankruptcy proceeding and was inherited by the trustee; that it was governed by the Oregon Statute of Limitations (Opinion of Judge Fee, Tr. p. 62 to 66).

Appellant has abandoned specification of error No. 1 which says that "the court erred in determining that the Oregon Statute was applicable," because the contention is not argued in the Brief. Appellant in effect concedes that in this jurisdiction, the law is that the State Statute applies as contended for by Appellee and as decided by the court below.

Appellant's counsel, after conceding that this court will probably so hold (Br. p. 23), states:

"We do not waive the point, but we shall not further discuss it (Appellant's Brief, p. 23)."

It is the general rule that a specification of error which is not argued will be deemed abandoned and will not be considered by the court.



**O'Brien's Manual of Fed. App. Pr., 3rd Ed., p. 212.**

**McCarthy v. Ruddock, 43 Fed. (2d) 976 (9th Cir.).**

**Forno v. Coyle, 75 Fed. (2d) 692 (9th Cir.).**

**Humphreys Gold Corp. v. Lewis, 90 Fed. (2d) 896 (9th Cir.).**

**Schroepfer v. Abell Co., 138 Fed. (2d) 111-116 (4th Cir.).**

In any event we believe there is no escape from the conclusion reached by Judge Fee upon this phase of the case (See opinion, Tr. p. 62-66 and authorities there cited).

**Section 1-201, Oregon Compiled Laws Annotated,** provides:

"Actions at law shall only be commenced within the periods prescribed in this title after the cause of action shall have accrued; . . . ."

**Section 1-206** provides:

"Within two years . . . . an action for . . . . any injury to the person or rights of another not arising on contract . . . . provided that in an action at law based upon fraud or deceit, the limitation shall be deemed to commence only from the discovery of the fraud or deceit."

**Section 9-103, Oregon Compiled Laws Annotated,** makes the foregoing statutes <sup>and</sup> limitations applicable to suits in equity.

Judge Fee predicated his decision upon the ruling of this court in **Davis v. Willey, 275 Fed. 397, 9th Cir.,** which affirmed the decision of the District Court, **263 Fed. 588.**

In a later case, **Meikle v. Drain**, 69 Fed. 2nd, 290, (9th Cir.), this court adhered to the ruling made in **Davis v. Willey**. It is interesting to note that Mr. Teiser, counsel for appellant in this case, was one of the attorneys in the Meikle case and it was there urged, in his Brief, that the ruling of this court in the **Davis case** was erroneous and should be overruled. This court declined to do so and reiterated its ruling in the **Davis case**. Because of these decisions, appellant's counsel now makes the admission that "this court would probably hold that the State Statute would still apply." (Br., p. 23).

In **Nairn v. McCarthy**, 120 Fed. 2nd, 910, the Circuit Court of Appeals for the 7th Circuit, followed the **Davis and Meikle** cases and went a step further. It held that Section 11(d) of the Bankruptcy Act (prior to Chandler Amendment):

"Does not grant an extension of time, but is a prohibition against the institution of actions either by or against the trustee subsequent to the designated time."

The court went on to say:

"It does not follow from the fact that the trustee is prohibited from bringing an action subsequent to that time that he is authorized to maintain an action prior thereto, irrespective of an applicable limitation statute. The provision is more for the protection of the trustee than for his benefit and, in any event, is for the purpose of terminating his duties and responsibilities . . . We are of the opinion that the State Statute of Limitation controlled . . . ."

On p. 23 of Appellant's Brief, the **Narin** case is erroneously listed as being opposed to the **Davis & Meikle** cases.

In **Herget v. Central National Bank & Trust Co.**, 324 U.S. 4-65, Sup. Ct. 505, the Supreme Court places the **Nairn** case in the group that supports the proposition that the State Statutes of Limitations applies to inherited causes of action.

The decision in **Harrigan v. Bergdoll**, 270 U.S. 560-46, Sup. Ct. 413, supports the ruling of this court in the **Davis and Meikle** cases. The court said:

"The Bankruptcy law . . . . does not modify this right of action against the stockholder or create a new one, it merely provides that the right created by the State law shall pass to the trustee and be enforced by him for the benefit of creditors."

The decision of this court also finds support in **Charlesworth v. Hipsch, Inc.**, 84 Fed. (2d) 834-837 (8th Cir.). The court there said:

". . . . time in which the trustee may sue can not be extended by a provision in the Bankruptcy Act which purports only to limit the time within which a suit may be brought by or against him. . . . ." (citing several cases).

In **Bovay v. Byllbsby**, 12 Atl. (2) 178 (Del.), the court held that an action by a trustee in bankruptcy to recover from officers and directors of a corporation monies fraudulently obtained, is "of a **dirivative nature**".

## V

**THERE IS ABUNDANT SUBSTANTIAL EVIDENCE TO SUSTAIN THE FINDINGS OF FACT NUMBERED III, IV, AND V, AND THE FINDINGS OF FACT SUSTAIN THE CONCLUSION OF LAW THAT THE ACTION IS BARRED BY THE OREGON STATE OF LIMITATIONS.**

## ARGUMENT

The alleged fraudulent transfer of the Consolidated Credit Corporation stock took place **December 12, 1929** (Tr. p. 6) and the Western Guaranty stock **December 20, 1930**, (Tr. p. 3).

Petition in Bankruptcy was filed November 25, 1931, (Tr. p. 2). Plaintiff was appointed Receiver August 13, 1934 and was appointed Trustee December 4, 1934 (Tr. p. 3). This action was commenced October 2, 1943 (Tr. p. 12).

The court below made findings of fact and conclusions of law on the issue of the statute of limitations (Tr. p. 73-74) quoted at page 4 of this brief.

The sole question is now whether there is **“any substantial evidence”** to sustain those findings of fact.

## General Principles Governing the Question as to What Constitutes Discovery of Fraud.

Under Sections 1-201 and 1-206, made applicable to suits in equity by Section 9-103, **Oregon Compiled Laws Annotated**, already quoted on page 31 of this brief, the statute of limitations bars an action for fraud two years after the cause of action accrues, and the cause of action accrues at the time of the discovery of the fraud.

In the **Linebaugh v. Portland Mtge. Co.**, 116 Ore. 1-8, the Oregon Supreme Court construed the provision as follows:

"The statutory provision that, 'the limitation shall be deemed to commence only from discovery of the fraud or deceit,' properly interpreted, means from the time the fraud was known or could have been discovered through the exercise of reasonable diligence;

. . . . .

"As stated in **Noyes v. Parsons, et al**, supra: 'Whatever is notice enough to **excite attention and put a party upon his guard** or call for an inquiry, is notice of everything to which such inquiry might have led.'"

This principle has never been departed from in Oregon and since the case involves the Oregon statute of limitations, we deem that ruling to be controlling.

The Oregon rule is in harmony with the rule laid down by the **Supreme Court of the United States** in the leading case of **Wood v. Carpenter**, 101 U.S. 135, and the rule laid down by this court in **Prentiss v. McWhirtier**, (9th Cir.) 63 Fed. (2) 712:.



In *Wood v. Carpenter*, *supra*, the Supreme Court said:

"Statutes of limitation are vital to the welfare of society and are favored in the law. They are found and approved in all systems of enlightened jurisprudence. They promote repose by giving security and stability to human affairs. An important public policy lies at their foundation. They stimulate to activity and punish negligence. While time is constantly destroying the evidence of rights, they supply its place by a presumption which renders proof unnecessary. Mere delay, extending to the limit prescribed, is itself a conclusive bar. The bane and antidote go together.

. . . . .

"Whatever is notice enough to **excite attention and put the party on his guard** and call for inquiry is notice of everything to which such inquiry might have led. **When a person has sufficient information to lead him to a fact, he shall be deemed conversant of it.**"

. . . . .

In *Avery v. Cleary*, 132 U.S. 604, it was held that this rule applies with greater force in bankruptcy proceedings because

"That object was to secure a **prompt determination of all questions arising in bankruptcy proceedings, and a speedy distribution of the assets of bankrupts among their creditors.**"

In *Prentiss v. McWhirtier*, *supra*, this court said:

"Under the cases in this state (California) it is not enough to assert that the discovery was not sooner made. It must appear that it could not have been made by the exercise of reasonable diligence; and all that reasonable diligence would have disclosed plaintiff is presumed to have



known, means of knowledge in such a case being the equivalent of the knowledge which it would have produced.”

**In 37 C.J. 976, the writer says:**

**“Ignorance of Details or Evidence—In General.—**It is not necessary that a party should know the details of the evidence by which to establish his cause of action. It is enough that he knows that a cause of action exists in his favor, and when he has this knowledge, it is his own fault if he does not avail himself to those means which the law provides for prosecuting or preserving his claim.”

**U. S. v. Christopher, 71 Fed. 2nd 764, 10th Cir.,**  
the court said:

“Discovery does not mean resort at leisure to known sources of information. Possession of the means of knowledge is tantamount of knowledge itself.”

In approaching the appraisal of the evidence it should be borne in mind that a trustee in bankruptcy is a quasi officer of the court (**Zimmerman v. Farmington Shoe Co., 31 Fed. 2nd, 405**). He is charged with the duty of collecting and recovering all property of the bankrupt for liquidation and distribution to creditors. He must exercise due diligence in this respect. If he fails to take proper steps to secure all assets he is presumably negligent and may be charged with the value of the assets lost. (re: Reinboth, 157 Fed. 627).

The Bankruptcy Act imposes upon a trustee in bankruptcy, the duty of making an examination of

the bankrupt. This duty is not imposed upon the trustee only when he has reason to believe frauds have been committed. It is his absolute duty to make an investigation into the affairs of the bankrupt to discover whether any fraudulent transfers were made.

**Section 47, Bankruptcy Act—11 U.S.C.A. 75.**

**Section 21(a) of the Bankruptcy Act—11 U.S.C.A. 44(a)**, affords the trustee in bankruptcy very effective facilities for the investigation of all of the transactions of the bankrupt. It authorizes the examination of “any” designated persons, including the bankrupt. The scope of the examination under this section of the bankruptcy act is very broad. The widest latitude is permitted. The examination can be “searching” and “summary”. The act authorizes examination in order to enable the trustee to ascertain whether there has been “fraudulent disposition” of the property and in connection therewith the production of books, papers and documents will be enforced.

(Vol. 5, *Remington on Bankruptcy*, (4th Ed.)  
Sections 1997 and 1998, and cases there cited  
in support of the text.)

In *Kinder v. Scharff*, 231 U.S. 517-34, Sup. Ct. 164, the court rejected the trustee's contention of lack of knowledge because he did not avail himself of the facilities for examination under **Sec. 21(a)** of the Bankruptcy Act. The Supreme Court affirmed the decision of the Louisiana Supreme Court which held (55 So. 769-711) that the alleged fraud would have been discovered if the examination under **Sec. 21(a)**

of the Bankruptcy Act had been conducted. The court said:

“ . . . . . A litigant who has voluntarily abstained from availing himself of the means put in his hands by the law itself for the ascertainment of a suspected fact cannot be allowed to plead his ignorance of such fact for arresting the course of the statute of prescription and repose. The law upon that point is fully settled.”

The urgency of a thorough investigation in this case was apparent because at the time of his appointment and even before, plaintiff knew that Farrington and others were under a cloud of suspicion that he had caused assets of the corporation to be fraudulently disposed of.

Judge Fee's summary of the pertinent facts in his opinion (Tr. p. 60-62) are clearly established by substantial evidence and sustain the findings of fact that plaintiff had knowledge and the means of knowledge, which if pursued would have disclosed all the pertinent facts pertaining to the transactions described in the complaint.

Even a cursory examination of the bankrupt's books would have disclosed that shortly prior to the filing of the bankruptcy petition, two large transfers of assets had been made (the transfers involved in this case.) One transfer was made less than a year prior to the filing of the petition in bankruptcy and the other less than two years prior thereto. These two transfers totalled in excess of \$140,000.00. They were unusual transactions and out of the ordinary course of business and therefore challenged attention

and investigation as a matter of course, particularly so because the entries disclosed that the Consolidated Credit Corporation stock was exchanged for the Keystone stock which was owned by the Western Bond and (Tr. p. 144) the Western Guaranty stock was not transferred for money, but was exchanged for other assets.

Plaintiff was an attorney (Tr. p. 84), and for ten years prior to his appointment as trustee, he was Chief of the Division of the State Tax Department and later Chief of the Income Tax Department of the United States Bureau of Internal Revenue (Tr. p. 97-98). He had considerable knowledge of accounting (Tr. p. 98) and in later years held himself out as an income tax counselor. (Tr. p. 103).

Plaintiff had available the facilities and assistance of (a) the Attorney General of the State of Oregon, (b) the Corporation Department of the State of Oregon, (c) two auditors of the Corporation Department without limit as to the services they were to perform (Tr. p. 190, 193, 194, 195, 196, 197), (d) he was paid a salary of \$150.00 a month by the State of Oregon and office facilities and office expense, (e) he had the assistance and advice of Mr. John Latourette, an attorney employed with the approval of the bankruptcy court for about one year, (f) and the assistance and advice of Mr. Teiser, present counsel (one of the ablest bankruptcy attorneys practicing at this bar) employed with the approval of the court, and (g) the services of the certified public accountant, Mr. Erickson, since 1936, who had contracted to render

services on all phases of the bankruptcy proceedings on a contingent basis. All this to aid in the investigation into the transactions which precipitated the bankruptcy and the recovery of assets alleged to have been fraudulently transferred.

Immediately upon his appointment he was made aware of the charges that were being asserted against Farrington and others.

Mr. Moody, Assistant Attorney General, called upon plaintiff immediately after his appointment as receiver (Tr. p. 190) and told him of the prior investigations that had been conducted and impressed upon plaintiff the importance of conducting the investigation. He called his attention to the newspaper accounts (Tr. p. 194) and the litigations in the state and federal courts charging Farrington with fraudulent transfer of assets including the transactions involved in this case. Mr. Moody made available to plaintiff the auditors of the Corporation Department (Tr. p. 193), and arranged for the payment to plaintiff of salary and expense by the State of Oregon (Tr. p. 195). Upon his appointment plaintiff came into possession of the books and records of the bankrupt company and its subsidiaries.

These were the auspices under which plaintiff entered upon the performance of his duties as receiver and trustee.



### **Transfer of Western Guaranty Stock**

To simplify presentation of this matter we will treat Farrington and Laurel Investment Company as a unit and as though the transactions were directly between Farrington and the Western Bond and Mortgage Company.

The vice in the Western Guaranty stock transaction as presented by the complaint and developed by the evidence is:

(a) That Farrington obtained from the Western Bond all of the capital stock of the Western Guaranty Company worth \$322,014.35; that Farrington caused to be transferred to the Western Bond as consideration therefor, the following assets:

1. 100 shares of capital stock of Lake Lucerne Company, a Washington corporation, without par value.
2. Conditional sales contract on automobiles with unpaid balances amounting to \$22,661.03.
3. Mortgage from Ljungdahl Products Co. to Massachusetts Mortgage Co., recorded in Records of Chattel Mortgage, Pierce County, Wash., amount of unpaid principal \$24,750.00.
4. Note, W. I. Birwell to Massachusetts Mortgage Co., dated October 6, 1930, \$19,477.70.
5. Note of Massachusetts Mortgage Co. to Laurel Investment Co. dated December 20, 1930, for \$87,000.00.



and that said assets were worthless. (Plaintiff's contention, pretrial order, Tr. p. 42).

(b) That Farrington obtained the assets which he transferred to the Western Bond as consideration for the Western Guaranty stock from Edward F. O'Flynn and his associates, or Massachusetts Mortgage Co., simultaneously with or shortly prior to the alleged transfer (Plaintiff's contention, pretrial order, Tr. p. 42-45).

The alleged fraudulent character of the transaction was summarized by plaintiff's witness Erickson, who claims to have discovered the alleged fraud as follows:

**"The material fact is that simultaneous character of these transactions, the use of the assets for two purposes simultaneously and the further fact that the assets were shown to have had no value." (Tr. p. 162).**

We deem the second contention to be wholly irrelevant, because if the Western Bond received assets of equal or greater value, then it was not damaged and neither the corporation prior to bankruptcy nor its trustee after bankruptcy would have any cause of action. And it is so conceded in the testimony. Erickson testified: **"If they did actually receive assets of value compared to what they parted with, they could not question the transaction."** (Tr. p. 160-161). It is obviously immaterial when or how or from whom defendant obtained the assets which were turned over to Western Bond in consideration for the transfer of the Western Guaranty stock, if said assets

were in fact of equal or greater value.

The only issue therefore, which can properly present itself now, is whether there is any substantial evidence to support the findings of fact that plaintiff had knowledge that the assets received in consideration were valueless or whether he could have by the exercise of reasonable diligence ascertained that fact more than two years prior to the commencement of this action.

The record establishes beyond question that **the transaction was spread upon the records of the corporation contemporaneously with its consumation.** The records of the corporation came into the possession of the plaintiff in the fall of 1934. (Tr. p. 131).

The "agreed facts" in the pretrial order (Tr. p. 21) recite that under date of December 15, 1930, the books of the Western Bond recorded the transaction whereby assets owned by Western Bond were transferred to the Western Guaranty Company, for all of its capital stock and the journal entries recording the transaction are set forth.

The "agreed facts", (pretrial order, Tr. p. 23) also recite that on December 20, 1930, at a special meeting of the directors of Western Bond, presided over by Farrington, O'Flynn and Johnson were elected directors; that the meeting recessed for a half an hour; that it reconvened; that defendant and others resigned as officers and directors; that the board then elected Johnson as president and O'Flynn as secre-

tary-treasurer; that a resolution was adopted (Tr. p. 24), authorizing the transfer to Farrington, (Laurel Investment Co.) all of the capital stock of Western Bond and in exchange therefore, to take an assignment from Laurel Investment Company, of the assets specifically described above which were enumerated and described in the resolution. It was further resolved at that meeting (Tr. p. 24), that in the judgment of the directors that the assets received by Western Bond in exchange for the stock of Western Guaranty: "are of equal or of greater value, than those so to be assigned to Laurel Investment Co. . . ."

The agreed facts also recite (Tr. p. 24) that on December 20, 1930, Laurel Investment Company transferred to Western Bond the assets specifically described above and received from Western Bond the stock of Western Guaranty.

Plaintiff testified (Tr. p. 96) that he inspected the main books of the Western Bond.

He knew that Farrington had sold his stock in the Western Bond in 1930 to Mr. O'Flynn, or the Massachusetts Mortgage Company, which he controlled, (Tr. p. 131), and that Farrington had retired as an officer and director after December 20, 1930. He testified, "I knew it from the corporation's records, yes." (Tr. p. 131).

Mr. Erickson, the certified public accountant, employed by the plaintiff in 1936, occupied offices in the same suite with Mr. Teiser (Tr. p. 140). He was first

employed by plaintiff in June or July of 1936, (Tr. p. 153).

Erickson testified (Tr. p. 157):

“Q. In respect to this Western Guaranty transaction, that whole transaction was set up on the books and in the journal and in the minute book, was it not?

A. There is a journal entry recording the disposition by the Western Bond and Mortgage Company of the stock in the Western Guaranty Company, for which they were supposed to have received certain assets, and there is a recital of the transaction in the minute book.”

He testified that the minute book shows that Farrington went out of the management and directorate and that O’Flynn and his associates came in (Tr. p. 158), and that the minute book shows that there was a meeting on December 20, 1930, when Farrington and McCroskey resigned and O’Flynn and someone else took his place; that there was an adjournment of 30 minutes and upon resumption of the meeting, the minutes “set forth the trade of the Western Guaranty stock for those other items which were supposed to have been received.” (Tr. p. 159).

He testified that the transaction is referred to at a later place in the minutes, some **two weeks later**, which shows there was a stockholders meeting at which the **transaction was ratified**. (Tr. p. 159-160). He testified:

“Q. So that the transaction was there for anybody to examine that wanted to?

A. What is recited there is easily read, yes.”

**He did not make any appraisal of the assets the Western Bond received in the transaction. (Tr. p. 160).**

He was asked what it was that he discovered in the books in addition to what is in them now in respect to this Western Bond transaction, (Tr. p. 161), and he answered:

**"The material fact is the simultaneous character of these transactions, the use of the assets for two purposes simultaneously and the further fact that the assets were shown to have had no value."**

The then testified that he discovered that the transactions were simultaneous in the Revenue Agent's report (Tr. p. 162).

At (Tr. p. 164) the testimony is as follows:

**"Q. Well, what you have discovered, then, was that the transaction, you claim, was simultaneous instead of an interval having elapsed, and that Farrington and Laurel Investment Company had acquired the assets that they used in that trade from the new owners of the Western Bond?"**

**A. That is what I found in the revenue agent's report, yes."**

**Q. And that is what you are relying upon as the newly discovered matter which you found out?"**

**A. Yes."**

But this alleged discovery is irrelevant because it is conceded that the only relevant fact was the value of the assets and **not the source or time of acquisition. (Tr. p. 160-161).**



He testified that the sources from which Farrington got the assets which he traded to the Western Bond for the Western Guaranty stock was **not a proper subject for entry on the books** of the Western Bond, **nor was the time** that elapsed between the acquisition of the assets and their transfer to the Western Bond **a proper matter to set up in the books.** (Tr. p. 165). **He found no changes in the books of the Western Bond with respect to the Western Guaranty transaction.** (Tr. p. 166).

Under his employment in 1936, he was to investigate the transaction relating to the Keystone ranch property:

“And to see what other items that might be on there that were subject to action by the trustee.” (Tr. p. 167).

He checked through most of the transactions of any consequence that pertained to the Bank of California matter, **“I put them aside and did not refer to them, I think, on no occasion until a long time later.”** (Tr. p. 167).

He was employed to investigate generally in the original employment. (Tr. p. 168).

In the course of his examinations, he called attention of the plaintiff and his attorney, to other transactions he had looked into. (Tr. p. 175).

If there was no other evidence in the record, the evidence thus far referred to would itself be ample to sustain the findings of fact made by the court below.



It is well settled that corporate books and records and account books to which a party has access, which give notice of the facts, are sufficient to charge interested parties with knowledge which the records would have disclosed and start the running of the Statute of Limitations.

In **Gibson v. Jensen**, 158, Pac. 426 (Utah), plaintiff's action was barred because he was a stockholder who had access to the corporate books and was found lacking in proper diligence in investigating the books. The court restated the principle that it was **not necessary that plaintiff be informed of all details** and that it was sufficient if she was informed of facts which would put an ordinary person of intelligence and prudence on inquiry.

In **Farmer v. Stendeven**, 93 Fed. 2nd, 959, 10th Cir., plaintiff was a receiver of a corporation. He sought to recover from its directors and officers, irregular profits on the sales of stock. The court held that the action was barred by the statute of limitations because the records of the stock transfers were reflected in the corporate books; that the receiver was chargeable with notice of what the books of the company reflected and what a reasonably prudent inquiry would have disclosed.

In **Noyes v. Parsons**, 177 Pac. 651 (Wash.), the suit by receiver was barred, because the receiver had possession of the corporate books and he was held chargeable with knowledge of the facts that could have been derived from the books. The court there

reiterated the principle that the party claiming to have been defrauded must be diligent in making inquiry and that **“means of knowledge are equivalent to knowledge. A clue to the fact which if followed up diligently would lead to a discovery, is in law equivalent to discovery—equivalent to knowledge.”**

In *Prentiss v. McWhirtier*, *supra*, this court held that the claim was barred by the statute of limitations because the plaintiff had access to the corporate records.

### **Re: Value**

There is not a scintilla of evidence in the record to explain why plaintiff could not have investigated in the fall of 1934, the value of the assets which were acquired by Western Bond, in exchange for the Western Guaranty stock. The assets were known. They were specifically identified, and were spread upon the records of the corporation. The value of those assets certainly could have been investigated in 1934 with greater certainty of ascertaining the truth than 15 years after the transaction. The identity of the assets were not concealed. No stumbling block was placed in the way of an investigation, and nothing was done to discourage an investigation.

Plaintiff asserts that the alleged fraud was not discovered until the receipt of the revenue agent's report in 1943. Under this allegation plaintiff had to establish that the revenue agent's report disclosed the facts showing that fraud was committed with

shortly prior to the filing of the bankruptcy petition. It called for investigation at that time. The very nature of the transactions excited attention and inquiry as to why the transactions were carried out and whether the corporation suffered detriment thereby. This at once called for an appraisal of the assets received. At the very time the trustee

reiterated the principle that the party claiming to have been defrauded must be diligent in making inquiry and that **“means of knowledge are equivalent to knowledge. A clue to the fact which if followed up diligently would lead to a discovery, is in law equivalent to discovery—equivalent to knowledge.”**

In *Prentiss v. McWhirtier, supra*, this court held that the claim was barred by the statute of limitations because the plaintiff had access to the corporate records.

### **Re: Value**

There is not a scintilla of evidence in the record to explain why plaintiff could not have investigated in the fall of 1934, the value of the assets which were acquired by Western Bond, in exchange for the Western Guaranty stock. The assets were known. They were specifically identified, and were spread upon the records of the corporation. The value of those assets certainly could have been investigated in 1934 with greater certainty of ascertaining the truth than 15 years after the transaction. The identity of the assets were not concealed. No stumbling block was placed in the way of an investigation, and nothing

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respect to the value of the assets.

The revenue agent's report, however, does not contain the slightest intimation of fraud in connection with the valuation of the assets received. On the contrary, the revenue agent's report accepts the valuation. They are not questioned. The report recognizes that Western Bond realized a profit of \$16,460.23 on the transaction and income tax was paid on that amount by the Western Bond (Appendix p. 9).

Erickson made no discovery of any fact relating to the value of the assets from the report or any other source and he made no appraisal of the assets. (Tr. p. 160). Nothing disclosed by the revenue agent's report caused Erickson or the plaintiff to make any appraisal of those assets, or to make any investigation as to the value.

We submit that there was urgent reason for investigating the value of those assets in 1934. The transaction was an unusual one. It was not a transaction in the ordinary course of business. When the trustee and his attorney and his accountant looked at those records (assuming that they did), they saw **an unusual transaction** by which a large block of assets were transferred to the Western Guaranty (which was formed for the purpose of receiving from them) in exchange for its stock and that the stock thus obtained was transferred in exchange for other assets. The value of the assets disposed of is alleged to be \$322,014.35. The transaction occurred ~~the assets received. At the very time that the trustee~~



obtained possession of those records he became charged with the duty of examining and investigating that transaction. **That was the incident that set running the statute of limitations** against him, because an investigation at that time into the value of those assets would have disclosed the only material fact that could possibly be the basis of this cause of action.

In **Beal v. Smith**, 189 Pac. 341, (Calif.), a stockholder sued the officers and directors of a corporation to recover from them secret profits which they derived from the transfer of securities owned by the corporation for alleged worthless stock. The court held:

“The very fact that such a large issue of securities was made in exchange for stock of unknown companies was sufficient to put a prudent man on inquiry.”

That is the very situation in the case at bar.

### **Re: First Revenue Agent's Report**

This report is plaintiff's Exhibit 59. It is reproduced so far as material in the Appendix of Exhibits (p. 1-9).

Plaintiff claims in his complaint, contentions in pretrial order and in the evidence in effect that it was the revenue agent's report that opened the vaults that disclosed the alleged fraud and the fraud he discovered was that Farrington acquired the assets which he transferred to Western Bond simultaneously with the transfer of the Western Guaranty stock to



him. (Tr. p. 162). He discovered nothing regarding the **value** of the assets. The report confirmed the valuation at which they were transfered to Western Bond.

The report is dated **October 12, 1932**, and it recites (p. 1) that the information contained in the report was obtained from **"an examination of the books and records of above named affiliated group."** A reading of the report confirms the fact that it purports to show **only what is in the books.**

We submit that plaintiff and his attorneys and his accountants could have obtained the identical information that the revenue agent obtained from the books and records which they had in their possession since the falls of 1934. They could have drawn the same inferences and conclusions as he did.

The facts pertaining to the Western Guaranty stock as narrated by the revenue agent in the report will be found on pages 8 and 9 of the Appendix of Exhibits. That portion of the report discloses the identical information that Erickson said was recorded in the books of the company, except of course, the **conclusions and inferences** that the revenue agent drew therefrom, that the **transactions were simultaneous.** The revenue agent **inferred** that the transactions were simultaneous because the minutes disclosed that on December 20, 1930, Farrington resigned as an officer and director and O'Flynn was elected as officer and director and that at the meeting, after a half hour adjournment a resolution was

adopted authorizing an exchange of the assets. Mr. Gunning in his report does not say that that is actually the fact. He merely says "the understanding apparently being that as soon as the new stockholders came into control of Western Bond", they would cause the company to trade the Western Guaranty stock to Laurel Investment Company for securities previously traded to Farrington. That was the conclusion which he drew from the books and minute entries. The plaintiff, his attorney and his accountant could have drawn the same conclusion. **The significant fact is that the report does not disclose any fact (as distinguished from conclusions) which was not found in the records.**

There is not the slightest intimation in the report that the conclusions were based on any other information than the corporate records.

Instead of disclosing fraud with respect to the only material fact (value), the report confirms the fact that the assets received were of greater value than the assets parted with.

### **Lack of Diligence in Obtaining Revenue Agent's Report**

We submit that the record establishes that plaintiff was lacking in diligence in obtaining the report. Plaintiff knew of its existence when the government filed the claim for additional income tax in 1935. Plaintiff tried to get a copy from the local office of the Internal Revenue Bureau at that time but was

advised they had none. He learned at that time that Mr. Robert T. Jacob, a tax attorney, had a copy. **He waited 3 or 4 years.** Then called at Jacob's office (Tr. p. 119) but did not obtain a copy because Jacob was away and he **never went back to that office again.** (Tr. p. 119). Mr. Teiser obtained a copy from the Internal Revenue Bureau in 1943 for the purpose of contesting the tax claim filed by the government in 1935.

Plaintiff asserts that he did not investigate the tax claim earlier because the referee in bankruptcy (now dead) "stated that there was no reason at that time to contest the claim" because there was no money on hand to pay the claim. But he did not **direct or state** that a copy of the report should not be obtained. He only stated that a contest be deferred.

Getting the report at that time would not have involved any effort or expense. He could have obtained it for the mere asking just as Mr. Teiser did in 1943.

Plaintiff was guilty of gross negligence in waiting from 1935 to 1943 to get a copy of the report. He did not exercise the degree of diligence required in order to prevent the running of the statute of limitations.

That report should have been obtained when its existence became known in order for the trustee to inform himself at least of the losses of the claim. He is charged with the duty **"to examine all proofs of claim and object to the allowance of such claims as may be proper."** (Sec. 47a-8 Bankruptcy Act—11 U.S.C.A. 75a-8). And he should have obtained the report in the performance of his duties to investigate

the affairs of the bankrupt (**Sec. 47a-7 Bankrupt**), for as a lawyer and accountant and from his experience in the Internal Revenue Bureau, he should have known that Internal Revenue reports frequently make disclosures with respect to bankrupts' property which set in motion pursuit of assets.

**Re: Consolidated Credit Corporation Stock Transfer**

It is alleged (Tr. p. 6) that Farrington fraudulently caused Western Bond to transfer to persons unknown, 40,000 shares of Consolidated Credit Corporation stock which Western Bond owned, in exchange for the capital stock of the Keystone Finance Company, **which Western Bond already owned.**

Plaintiff stated the issues in substantially the same terms in the pretrial order. (Tr. p. 25).

Plaintiff's case establishes that the transaction was spread upon the Western Bond books exactly as alleged in the complaint. Plaintiff's accountant, Erickson, testified (Tr. p. 144) that there is an entry on the books of the Western Bond recording the transaction which recites Western Bond parted with 40,000 shares of the Consolidated stock for which it received 1500 shares of Keystone stock "and the figures are of equal value, for what was parted with and what was received."

Since this entry was in the books in the possession of the plaintiff, he was, of course, chargeable with knowledge of it even if he had not looked at it. But it appears affirmatively from plaintiff's case that



Erickson, the accountant, saw the entry in 1936 (Tr. p. 145-167) in the course of examination of the records, at Mr. Teiser's request who "engaged me to assist him in tracing out the entries on the books." Mr. Teiser had "this matter of **exchange of the Keystone ranch property**" and "to see what other items might be in there that were subject to action by the trustee."

Having found the transaction on the books he "put them aside" and did not refer to them "on any occasion until a long time later." (Tr. p. 167).

He testified he did not discover anything questionable about the transaction. **But the entry itself suggests that the transaction is questionable. The entry records the very fact which plaintiff now complains about, namely—that Western Bond got no consideration because it was already the owner of the Keystone stock** (Tr. p. 6).

Plaintiff himself examined the "main books" of the Western Bond in 1934. (Tr. p. 96). He had the Keystone stock book in 1936. (Tr. p. 131-132).

In 1936, plaintiff commenced the litigation against the Bank of California to recover the value of the "Keystone" or "Russell" ranch as it is interchangeably referred to, on the grounds that the bankrupt obtained the ranch from Western Bond after the filing of the bankruptcy petition; that Western Bond was the owner of the ranch, although title had been in the Russell Land and Livestock Company, and by it transferred to Keystone Finance Company, because these

two were "wholly owned subsidiaries" of the Western Bond. **Plaintiff so alleged in that proceeding in 1936 (Ex. 103-103a, Appndx. 94-96), and it was so adjudicated by Judge Fee (Appndx. 105-108, 44 Fed. Supp. 89) and by this court (132 Fed. 2nd, 769).**

This evidence establishes conclusively that plaintiff had knowledge since 1934 and certainly since 1936 of the **very fact which the complaint now charges constituted the fraudulent transaction and** certainly started the running of the statute of limitations.

During the trial, Erickson stated the vice in the transaction in a different way. (Tr. p. 168-169). He said that parties named Tapfer and Snodgrass conveyed title to the Russell ranch in payment for all of the capital stock of the Keystone Finance Co.; that in fact Tapfer and Snodgrass had no title, therefore, Keystone did not acquire the title and hence the transfer of the Keystone stock to Western Bond did not give the Western Bond anything of value; that the title was owned by a man named Russell; that in 1925 he conveyed it to Russell Land and Livestock; that Western Bond owned the stock of the Russell Land and Livestock Company, therefore, Western Bond was already the owner of the ranch by virtue of the stock ownership of the stock of Russell Land and Livestock Company.

The complaint about that transaction is not that the property did not equal or exceed in value the Consolidated Credit Corporation stock but involves



merely the title to the ranch at the time of the transfer. That is the gravamen of that controversy as narrated by Erickson. (Tr. p. 168-169). The only question that presents itself in this respect is whether plaintiff is chargeable with knowledge of those facts and if he did not have actual knowledge whether he could have discovered these facts by the exercise of reasonable diligence more than two years prior to the commencement of this action.

The complaint alleges that the "true character" of the transactions was discovered by the accountant who made an investigation and discovered the facts referred to after the revenue agent's report was obtained.

The testimony of the accountant, Erickson, discloses, however, that the revenue agent's report did not disclose any facts relating to ownership of the ranch. (Tr. p. 184). On the contrary, he said that he obtained this information from

- (a) The account books of Western Bond. (Tr. p. 144).
- (b) The minute book of Keystone Finance Co. (Tr. p. 148).
- (c) The abstract of title. (Tr. p. 148).

The minute book disclosed that Tapfer and Snodgrass paid for their stock by conveying the Russell ranch (Tr. p. 168-169). The abstract of title disclosed that Tapfer and Snodgrass never had any title. (Tr.

p. 169). And the account books disclosed that the Consolidated stock was traded for the Keystone stock.

The accountant testified (Tr. p. 144) that the transfer of the Consolidated Credit Corporation stock in exchange for the Keystone stock was recorded in the books of the Western Bond and and the entries show that the figures are of equal value (the question of value is not involved in this transaction).

He saw the entries when he examined the books in 1936 (Tr. p. 145 and 167) when he was examining into the Bank of California transactions, "I put them aside and did not refer to them, I think, on no occasion until a long time later." (Tr. p. 167).

He testified that he "discovered" from the abstract of title that Tapfer and Snodgrass were never the owners of the property and that therefore Keystone acquired no title by conveyance from them. (Tr. p. 168) and that Russell Land and Livestock Co. was the owner in 1925. (Tr. 168).

At Tr. pp. 183 and 184, his testimony is as follows:

"Q. Did you or did you not discover the situation in regard to the 40,000 shares of stock, the Consolidated Company stock, at any time prior to 1943?

A. Oh, yes. I saw the record of the transaction, I think, probably in 1936."

. . . . .

"Q. This minute book of the Keystone Finance Company has been in the files of the Western Bond and Mortgage Company, since you have known anything about those files?

A. I think it was in there in 1936, yes. I am

sure it was.

“Q. Any investigation of the minutes of the subsidiary corporation would disclose the basis for the stock subscription concerning which you speak?

A. Yes, sir.”

Erickson said he examined the abstract of title in the spring of 1943 in connection with the purchase of the property by a client of his office (Tr. p. 147).

The fact is, however, that the abstract of title was **available for inspection at least since 1936**. At that time, Mr. Teiser had the abstract of title during the trial of the Bank of California case. It was produced during the examination of witness Greene in that proceeding (Exhibit 103, Appendix 109).

Of course, the abstract of title disclosed what was already a matter of **public record** available to all. It is a summary of the instruments affecting the title in so far as they are recorded in the office of the county clerk and recorder. The records are required by law to be kept and everyone is of course, chargeable with at least constructive notice of those public records.

Where the facts constituting or showing the fraud, appear from the public records required by law to be kept, and open for inspection, plaintiff's ignorance of the fraud will not postpone the operation of the statute of limitations.

37 C.J. 943.

34 Am. Jur. 137.

**Section 47(<sup>c</sup>) Bankruptcy Act—11 U.S.C.A. 75(<sup>c</sup>)**  
provides:

“The trustee shall, within ten days after his qualification, record a certified copy of the order approving his bond in the office where conveyances of real estate are recorded in every county where the bankrupt owns real property or an interest therein, not exempt from execution, and pay the fee for such filing.”

This mandatory requirement makes it incumbent upon the trustee in bankruptcy as soon as he is appointed, to make diligent inquiry as to the ownership of real property by the bankrupt so that he can perform the function commanded by this statute.

The ownership of the ranch and relationship between Western Bond, Keystone and Russell Companies as of the day of the filing of the petition in bankruptcy was the very foundation of the summary proceedings prosecuted by the plaintiff against the Bank of California. (See proceedings in **McBride v. Bank of Calif., Plaintiff's Ex. 103 and 103A, Appendix p. 95 to 138 and decision by Judge Fee, 44 Fed. Supp. 89 and the decision by this court, 132 Fed. 2nd 769.**)

We submit that the record in that case constitutes ample substantial evidence to support the findings that plaintiff could have discovered the fact as to ownership of the ranch and relationship of the corporations, from sources of information available to him more than two years prior to the commencement of this suit.

We defer discussing the additional evidence at this point because it relates to both transactions and, therefore, will be discussed later.

The very nature of the transaction called for scrutiny. The fact that the corporation parted with an asset of large value alleged to be worth \$120,000 (Tr. p. 6 and 7) and that it was exchanged for the stock of the Keystone Company, a corporation which was already owned by the bankrupt, in and of itself at once suggested inquiry as to the bona fides of that transaction (**Beal v. Smith, supra**). Any inquiry into the transaction at that time would have disclosed the very same information which the accountant claims to have discovered in 1943 because he got his information from the account books, minute book and from the abstract.

When the trustee looked at the record of the transaction on the books of the company showing that the Consolidated Credit Corporation stock was transferred in exchange for the Keystone stock (assuming that he did examine that record), he was bound to know at once that there was something wrong for he knew at that time, or so he claimed that the bankrupt already owned the Russell Ranch through the medium of the Russell Land and Livestock Company, and, therefore, the transfer of the Keystone stock was meaningless as consideration. He was then put on notice, or would have been put on notice had he examined the record, which prompted further investigation into the source of title to the Russell ranch.



Judge Fee, who tried this case, also rendered the judgment in the Bank of California case and much weight must be given to his understanding of the issues involved in both cases. He was convinced that the questions tried in the Bank of California case charged the trustee with the duty of further inquiry into the question of the source of title to the Russell ranch and he so indicated in no uncertain terms as is evident from the colloquy between Judge Fee and the accountant Erickson, who claimed to have unearthed the so-called alleged fraud. (Tr. p. 178 to 183).

Judge Fee very properly pointed out to Mr. Erickson during the colloquy (Tr. p. 181):

“I do not quite see what the purpose of that was, and it is not clear to me what part of this transaction that you are now examining was not clear to you through your investigation of The Bank of California transaction.”

But whatever question there might lurk as to when knowledge could have been obtained, was certainly dispelled by Erickson's concluding testimony. (Tr. p. 184). He testified:

“Q. This minute book of the Keystone Finance Company has been in the files of the Western Bond and Mortgage Co. since you have known anything about those files?

A. I think it was in there in 1936, yes. I am sure it was.

Q. Any investigation of the minutes of the subsidiary corporation would disclose the basis for the stock subscription concerning which you speak?

A. Yes, sir.”



Here is a complete dissipation of the contention that the trustee was without means of knowledge.

**Re: Judicial Proceedings in State and  
Federal Courts**

Defendant's Ex. 62, Appndx. p. 16, is a complaint filed in the United States District Court of the State of Oregon, on **March 13, 1931**, by John Brockie, against **Western Bond, Farrington** and others.

It alleges that Farrington controlled the Western Bond and many subsidiaries including Western Guaranty, Keystone Finance, and Russell Land and Livestock Co. The complaint specifically charges that Farrington, along with others, misappropriated the Western Guaranty stock. The transaction is described in great detail in Par. IV of that complaint (Appndx. p. 18-20 and thereafter).

The Brockie complaint describes in detail the **five items of assets** which Farrington transferred to the Western Bond in consideration for the Western Guaranty stock (Appndx. p. 20) and **it is there alleged that these assets were worthless** (Appndx. p. 20 and 21). **This is the very heart of the charge in the case at bar.**

The answers interposed by Western Bond (Appndx. p. 33) and Farrington (Appndx. p. 43) put in issue all the material allegations of the complaint and alleged affirmatively that the assets transferred were of equal or greater value than the Guaranty stock. (Appndx. p. 39).

Appellant seeks to avoid the effect of this judicial

record because the suit was dismissed on August 18, 1931. We fail to see any significance in that fact. The entry of the order of dismissal **did not expunge the papers from the files**. The records were still there to be seen by those who would take the trouble to examine them.

It is important to note, however, that the order of dismissal was entered upon plaintiff's own motion and was **"without prejudice."** (Appndx. p. 63). The legal implication is that the plaintiff **reserved** the right to commence another proceeding to enforce the rights asserted in that proceeding. It is not like a judgment entered after a trial on the merits dismissing the complaint, which would carry with it the conclusion that the issues were determined adversely to the plaintiff.

This judicial record charged plaintiff with knowledge of facts which if investigated would have led to the discovery of the facts pertaining to the transaction set forth in the complaint and therefore started the running of the statute of limitations against him.

Ex. 88, Appndx. p. 82, is the complaint filed November 21, 1931, in the Circuit Court of the State of Oregon by H. C. Thompson and others against Western Bond and Mortgage Co.

Ex. 87, Appndx. p. 90, was an order allowing an inspection of the books and records of the Western Bond and Ex. 88, Appndx. p. 92, is the affidavit filed in support of the motion for inspection.

Farrington was not made a party defendant to

that suit. However, the suit was against the Western Bond and in that complaint **Farrington** is charged with the same misconduct as in the Brockie case and in the case at bar, and it deals specifically with the December 20, 1930, transaction. (Appndx. p. 84-86). It alleges that he was in control of the Western Bond and of many subsidiary corporations including the Western Guaranty Co., Keystone Finance Co., Russell Land and Livestock Co., Laurel Investment Company and others.

This judicial record discloses that an order for an inspection of the books and records of the Western Bond was made, but no investigation was made into the facts disclosed by the inspection. The affidavit of Mr. McCurtain, filed in support of that order (Appndx. p. 92), disclosed that he had an audit made of the books and records of Western Bond, but no effort was made to ascertain what that audit disclosed. The complaint and the audit would have led plaintiff to a discovery of the facts pertaining to the transactions referred to in the complaint and that judicial record is sufficient to start running the statute of limitations.

There was another proceeding brought in the State court by Pape and others about the same time in which substantially the same charges were reiterated.

**Plaintiff and his counsel knew of those proceedings.**

In plaintiff's statement of his contentions in the

pretrial order (Tr. p. 49), he states:

**“He had a general knowledge that charges had been made and suits or actions brought both in the federal and state courts, against the Western Bond and Mortgage Company previous to his trusteeship herein in 1934, and that some charges in some of said suits or actions had been made against C. H. Farrington, but as to the nature and details of said charges plaintiff was not informed, nor did he have knowledge thereof.”**

The lack of knowledge of the details of the alleged fraud will not prevent the running of the statute of limitations (37 C.J. 976, Section 359). Since he had knowledge of the judicial proceedings and that they contained charges against the defendant, it was his duty to examine those proceedings and had he done so, he would have found spread upon those records the very charges which he now asserts in this case. That is particularly true in the **Brockie case** (Appndx. p. 16-26).

Counsel for appellant as a witness in this case testified that he knew of the **Thompson case** and that he talked to Allen McCurtain, attorney for the plaintiff in that case, about it. (Tr. p. 215). The Thompson case was brought into question during the litigation in the Bank of California case (Tr. p. 216), but he did not make any investigation of those complaints (Tr. p. 217).

During the trial of the Bank of California case in 1936, Mr. Teiser questioned the witness Thomas G. Greene about the Brockie case. He knew that Col. Clark was the attorney for the plaintiff in the Brockie

case. (Tr. p. 220). This was on November 9, 1936 (Tr. p. 220), but the charges made in those proceedings were not investigated.

The plaintiff himself knew of the judicial proceedings. The Assistant Attorney General, Mr. Moody, called Mr. McBride's attention to the newspaper articles that gave a great deal of publicity to the proceedings. (Tr. p. 194). He did that at the very inception of McBride's appointment in the fall of 1934.

Indeed it is not argued in appellant's brief that appellant and his counsel were not aware of the judicial proceedings in the state and federal courts.

Appellant asserts (br. p. 30) "the pleadings in neither of these cases (Thompson and Pape) even remotely referred to the fraud here alleged." The record contradicts that statement. The amended complaint in the Thompson case (Ex. 86, Appndx. p. 82) charges that Farrington was in control of Western Bond and a large number of subsidiary companies, including the Laurel Investment Company, Keystone Finance Company, Russell Land & Livestock Company. He is charged with "juggling the assets" and Par. VII, p. 84, specifically deals with the transaction which took place December 20, 1930. It charges the "abstraction" on that date of assets worth \$300,000.00 and transfer of those liquid assets to Farrington and Laurel Investment Company (Appndx. p. 86).

With respect to the **Brockie case**, appellant merely argues (p. 30) that if the trustee had examined the records in that case, he would have discovered that



the suit had been dismissed and therefore, as an ordinarily prudent man, he would have ceased further inquiry.

There is, of course, implied in that argument, the admission that he did not examine the records in the Brockie case. Of course, if he had examined the record, he would have discovered not only the order of dismissal "without prejudice", but he also would have discovered the more important fact that Farrington was being charged with fraud in connection with the **very same transaction** (Western Guaranty stock) that is involved in the case at bar. He would have seen that as easily as the order of dismissal. The performance of the plaintiff's duty as trustee demanded that he follow up the charges made in that proceeding and to ascertain the facts pertaining thereto, for it involved the transfer of assets in excess of \$300,000.00 **shortly prior to the filing of the petition in bankruptcy**. No effort is made to disclaim knowledge of the existence of the litigations.

In *Pearsall v. Smith*, 149 U.S. 231, 13 Sup. Ct. 833, an assignee in bankruptcy was charged with knowledge of a litigation commenced eleven years before the commencement of the action by the trustee notwithstanding the fact that the trustee only acquired knowledge of that litigation about two months prior to the commencement of his action to set aside fraudulent conveyances. The court said:

"In the present case the deeds of conveyance by Smith were recorded. **The suit by the Kittels was a public suit.**"



In **Lampor v. Osious**, 38 Fed. Supp. 373, the trustee in bankruptcy was charged with knowledge of the judicial records in prior litigations.

In **Bainbridge v. Stoner**, 106 Pac. 2nd 423 (Calif.), the plaintiff was charged with knowledge of the facts disclosed by other judicial proceedings.

In **Feak v. Marion Steamshovel Co.**, (9th Cir.), 84 Fed. (2) 670, this court charged the plaintiff with knowledge of facts disclosed by other judicial proceedings involving the same property.

### **Re: Public Knowledge Through Newspaper Publications**

We recognize, of course, that an isolated newspaper account of some occurrence will not charge an ordinary person with knowledge of the transaction. But, that is not true in cases where a great deal of publicity is given to a transaction in newspapers of general circulation.

In this case, the articles were numerous. The attention of the plaintiff was **specifically directed to these newspaper accounts** by Assistant Attorney General Moody immediately after plaintiff's appointment as receiver and subsequent thereto. Mr. Moody arranged that whenever there were any newspaper accounts pertaining to the affairs of the Western Bond that there were to be clipped and turned over to him and he in turn relayed them to the plaintiff (Tr. pp. 194-199). There is a large folder full of newspaper clippings in evidence (Paintiff's Ex. p. 162, Tr. p. 266).

We have printed excerpts from a number of these newspaper clippings (Appendx, pp. 30, 31, 32, 64, 66, 69, 71, 74, 76, 77, 78, 80, 81). They are replete with reference to the court proceedings charging fraud against Farrington. As for example (Ex. 64, Appndx. p. 31), the article dated March 13, 1931, recites that in the Brockie suit it is charged that Farrington through an intricate network of dummy companies abstracted more than \$300,000.00 worth of assets of the firm.

Ex. 75, Appndx. p. 64, recites the filing of the Thompson suit and that it is charged therein that Farrington and O'Flynn and others entered into a conspiracy to abstract assets in the sum upwards of \$300,000.00. To the same effect are all the newspaper articles introduced in evidence. Plaintiff's counsel had the whole sheaf of newspaper articles in his possession in the Bank of California case in 1936, and he examined the witnesses in reference to those articles. (Tr. pp. 225 to 239). He examined Thomas G. Greene particularly in reference to the credit file (Ex. 162) which contains a great many of the articles (Tr. p. 230 to 237).

It is highly significant that in 1936, Mr. Teiser attempted to charge Thomas G. Greene, attorney for the Bank of California, with knowledge of the facts conveyed by these newspaper articles, but now, counsel insists that they conveyed no notice to him or to the plaintiff.

We submit that the articles were so numerous and

were of such a character that they charged plaintiff with knowledge of all the facts that would have been discovered had he investigated the charges made therein. This was particularly his duty because Mr. Moody had specifically called it to his attention for that very purpose. These articles, therefore, started the running of the statute of limitations.

General public information has been held sufficient to charge a litigant with notice and start the running of the statute of limitations.

In *Stone v. Winn*, 176 S.W. 933, a taxpayer sued for an injunction to enjoin the fiscal court from levying a tax to pay bonds that had been previously issued. The suit was predicated on fraud in the election which approved the bonds. The Kentucky court held that the suit was barred by the statute of limitations since the claim of fraud was a matter of **public information** in that county which started the running of the statute.

### **Information Imparted to Plaintiff by Assistant Attorney General Moody**

The record discloses as soon as plaintiff was appointed receiver, Mr. Ralph Moody, Assistant Attorney General of the State of Oregon, called on plaintiff and informed him of the prior investigations made by the office of the Attorney General and the Corporation Commissioner; of the great concern that they had over the disposition of the assets of the corporation, and that Farrington was being accused of the unlawful transfer of assets. Mr. Moody called plain-

tiff's attention to the newspaper accounts of several litigations in which charges of fraud were made against Farrington and urged an extensive investigation into the civil and criminal liability of Farrington and all others who might be responsible.

We submit that this information coming from a high state official, coupled with the duties the Bankruptcy Act itself imposed upon plaintiff, was sufficient to charge plaintiff with the realization of the gravity of the situation and required more than ordinary diligence and scrutiny in investigating the affairs of the corporation. This information made it absolutely necessary for plaintiff to investigate at least the **major transactions** resulting in the transfer of assets **within a short period of time prior to the filing of the Petition in Bankruptcy** which would have included the two transactions involved in this case. One took place less than two years prior to the filing of the Bankruptcy Petition and the other less than one year prior thereto. These two transactions resulted in a transfer of assets alleged to be a total of over \$440,000 and certainly were large enough and of sufficient importance to challenge attention and scrutiny and fullest investigation into (a) the value of the assets received in exchange therefor, and (b) any other factors affecting the good faith of the transaction. We say, therefore, that the information imparted to plaintiff by the Assistant Attorney General was a fact potent to start running the statute of limitations, for so grave was his concern and so insistent was he upon a thorough investigation that they provided for



the payment of a salary by the State of Oregon to the receiver as well as supplying him with office space and office expense, a most unusual procedure.

**Re: Concealed, Camouflaged, Misleading and False Entries on the Books**

The complaint attributes delay in discovering the alleged fraud to concealed, camouflaged, misleading and false entries on the books of Western Bond and Mortgage Co. (Tr. p. 7).

We submit that there is not a scintilla of evidence in the record to sustain this allegation. Appellant does not in his brief point to a single item of evidence in support of the allegation. **There is no such finding of fact.** On the contrary, the accountant, Erickson, testified that Western Guaranty transaction was spread upon the records and he does not point to a single false entry in connection therewith. The records disclosed the transfer of assets from Western Bond to Western Guaranty in exchange for its stock, the transfer of the Western Guaranty stock to Farrington, and the consideration received therefor. The valuation placed upon the assets was also recorded in the minutes of the board of directors by the resolution that the value of the assets received were equal to or greater than the assets transferred. The only entries which plaintiff claims are not recorded in the books are:

- (a) The source from which Farrington obtained the assets which he transferred in consideration for Western Guaranty Stock.

- (b) The time that elapsed between their acquisition and the transfer to Western Bond.

As to these facts the accountant, Erickson, testified that they do not properly belong upon the books of the Western Bond. (Tr. p. 165). That is obviously so because those two facts relate to the transaction between Farrington and O'Flynn, *inter se*, **They do not relate to a transaction to which Western Bond was a party.**

The transfer of the Consolidated Corporation stock was likewise spread upon the records of the Western Bond. There is not a word of evidence of the concealment of any fact in relation to that transaction. As far as the Western Bond was concerned the transaction consisted of the transfer by it of the Consolidated stock and the receipt by it of the Keystone stock. These entries were recorded.

Here to, appellant's brief does not point to a single item of evidence of any thing that should have been recorded which was omitted. Neither does it point to any entry in the books that is erroneous in this respect much less false.

### **Re: Lack of Funds to Finance Investigation**

Appellant attempts to excuse the failure to investigate the affairs of this corporation and particularly the alleged frauds charged in the complaint by the repeated assertions that the estate did not have much money and that the small amount of money was earmarked for investigation and prosecution of



the Bank of California suit. (appellant's brief p. 26 and 27). We know of no reason why funds should be earmarked for the investigation of one transaction any more than another.

In any event, it is settled beyond question that the lack of funds or even poverty which prevents investigation will not prevent the running of the statute of limitations.

**Leggett v. Standard Oil Company, 149 U.S. 287.**  
**Cummings v. Wilson & Willard Mfg. Co., 4**  
**Fed. 2nd 453, 9th Cir.**

**Gillons v. Shell Co., 86 Fed. 2nd, 600, 9th Cir.**

**Baillie v. Columbia Gold Mining Co., 86 Ore.**  
**1-22.**

Lack of funds did not account for the failure to investigate, because plaintiff was given the services of two expert auditors from the Oregon Corporation Department without limit, he was paid a salary of \$150.00 per month and office expense by the state, and from the middle of 1936 he had the services of the certified public accountant who agreed to render his services on a contingent basis to investigate all matters.

Moreover, no expense was needed to discover the pertinent facts. The Western Guaranty stock transaction only involved the question of the value of the assets received which were spread on the books and the Consolidated Credit Corporation stock involved the ownership of the Russell ranch which was ascertainable from the abstract of title.

**Re: Knowledge Obtained by Counsel for Plaintiff**

Plaintiff was chargeable with knowledge of all the facts or information which was obtained or came into the possession of his counsel, Mr. Latourette and Mr. Teiser.

It is a well recognized rule that knowledge of facts relating to the subject matter of the employment acquired by an attorney while he is engaged in the discharge of his duties under the employment is imputed to his client. (See cases annotated—4 A.L.R., 1594 and 38 A.L.R. 820. The same rule is set further in 5 Am. Jur. p. 302, section 74.)

**CONCLUSION**

We submit that judgment appealed from should be affirmed because:

- (a) Appellant's Specification of Errors do not raise any issue with respect to the sufficiency of evidence to sustain the findings of fact upon the issue of laches and if that contention be sustained all other questions become moot.
- (b) Assuming without admitting that the issue of laches is properly before the court for review, the record establishes that there is a great abundance of evidence to sustain the findings of fact upon which the court below applied the doctrine of laches.

If the court holds that the suit is barred by laches, the question of the application of the statute of limitations becomes moot.

- (c) There is an abundance of evidence to sustain the findings of fact of the court below upon which it made its determination that the action was barred by the statute of limitations.

Respectfully submitted,

S. J. BISCHOFF,  
Attorney for Appellee.



No. 11116

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In the United States

# Circuit Court of Appeals

For the Ninth Circuit

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,

*Appellant,*

vs.

C. H. FARRINGTON,

*Appellee.*

---

## APPENDIX OF EXHIBITS

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Upon Appeal from the District Court of the United  
States for the District of Oregon.

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J. J. BISCHOFF,

Spalding Building,  
Portland, Oregon,

*Attorney for Appellee.*

FILED

1915

PAUL H. GORDEN,

CLERK





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In the United States  
**Circuit Court of Appeals**  
For the Ninth Circuit

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,

*Appellant,*

vs.

C. H. FARRINGTON,

*Appellee.*

---

**APPENDIX OF EXHIBITS**

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Upon Appeal from the District Court of the United  
States for the District of Oregon.

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## PLAINTIFF'S EXHIBIT NO. 59

### FIRST REVENUE AGENT'S REPORT

File No. 4277-0.

Examining Officer:  
L. C. GUNNING

Time spent on examination: 23 Da

Portland, Oregon

In re: WESTERN BOND & MORTGAGE COMPANY  
October 12, 1932.

70 Broadway  
Portland, Oregon.

Present Name & Address:  
WESTERN BOND & MORTGAGE  
COMPANY

Internal Revenue Agent in Charge  
Seattle, Washington.

302 Guarantee Trust Building,  
Portland, Oregon.

An examination of the books and records of the above-named affiliated group for the calendar year 1930, disclosed the following in connection with its income tax liability:

#### SUMMARY

Years	Additional Tax	Penalties	Filing District
1929	Net loss verified	5% Negligence	OREGON
1930	\$46,838.56	\$2,341.93	

Net Additional Tax: \$46,838.56—Penalty \$2,341.93.

Nature of business: Financial, Real Estate, Etc.

Authority for examination: Original return 1930.

Comparison has been made with same.

Waivers: None. Claims: None.

Correspondence from the Bureau: None.

Authority for departing from manual: Complied.

Class 4 Report.

Basis for Consolidation:

The parent company owned all of the outstanding stock of the following companies:

Inclosures: Original Return 1930

Western Bond & Mortgage Guarantee Co.	Liquidated 1930
Broadway Oak Corporation	" "
Livestock Investment Co.	" "
Keystone Finance Co.	" "
Livestock Loan Co.	" "
Russell Land & Livestock Co.	" "
Central Realty Co.	" "
Western Insurance Agency, Inc.	" "
Beacon Investment Co.	" "

Form No. 1122 were filed for each of the above corporations. Form 851 revised was properly executed with the exception it does not show the dates upon which the above companies were liquidated.

Investigation revealed that this company also owned the stock of the Consolidated Finance Company of Washington and the Northwestern Finance Company for part of the year 1930. These stocks of these two companies were acquired in the later part of January 1930 and were sold in the early part of February 1930. Since these stocks were held less than thirty-one days, and since the above companies were not included in the original consolidated return filed it is presumed that the taxpayer exercised the option granted to it by Article 13 (f) Regulations 75 and excluded the operations of these companies for the period owned from its consolidated income.

In the liquidation of the above companies during 1930 the parent company incurred both profits and losses which it included in its income and deductions on the return. The gains and losses on liquidations have been eliminated from the consolidated income in accordance with Article 37 (a) Regulations 75.

#### Other Information:

Taxpayers return sets forth losses on the sales of the stock of several different companies. See Schedule F of the original return.

Investigation showed these losses to be incurred in transactions between itself and the Consolidated Credit Corporation, a corporation which was under the control of C. H. Farrington, who was also the principal stockholder of the Western Bond & Mortgage Co. These transactions were reflected on taxpayers books and upon the books of the Consolidated Credit Corporation by a series of complicated book entries, and it was necessary to spend several days in analyzing the entries on the books of both companies to determine just what took place.

The books of the Western Bond & Mortgage Company show that in 1929 it was instrumental in forming a company known as the General Loan Company.



The purpose of this company was to engage in the small loan business. The original capital was \$15,000.00 which was subscribed for by the Western Bond & Mortgage Company. The name of this company was later changed to the Consolidated Lenders of Oregon and from that to the Consolidated Credit Company.

In 1929 another company was formed. This company was known as the Consolidated Credit Corporation. The purpose of this company was to be a holding company, the object of which was to gain control of a number of companies already engaged in the small loan business.

The stock of the Consolidated Credit Corporation was divided into three classes namely:

Preferred Stock \$10.00 par value.

Common Stock Class "A" No par value.

Common Stock Class "B" No par value.

The Class "B" Common was the voting stock and was all subscribed by C. H. Farrington, Bennett Baldy and R. E. Vester. Farrington held the majority of the stock and the control of the corporation.

The Western Bond & Mortgage Company subscribed for \$300,000.00 worth of the Class "A" Common and gave in payment therefor \$300,000.00 in notes receivable of several livestock companies. It appears from the circumstances that these notes were of little or no value at the time, the Consolidated Credit Corporation never received any payment on any of these notes from the makers but by a series of transfers and substitutions rid itself of them at the expense of the Western Bond & Mortgage Company.

The Consolidated Credit Corporation purchased the 150 shares of outstanding stock of the Consolidated Credit Company from the Western Bond & Mortgage Company, at a purported price of \$75,000.00. This transaction was reflected on its books by the following entry.

Dr. Corporation Stocks

owned .....\$75,000.00

Cr. Cash (Western Bond &

Mortgage Co.) .....

\$28,500.00

Livestock Loans .....	46,500.00
J. S. Hill.....\$	3,500.00
Grand Ronde L. S. Co. ....	43,000.00

To record purchase of 150 shares of the capital stock of Consolidated Credit Company.

The books of the Western Bond & Mortgage Company reflect the cash part of the above transaction and show a profit on this sale of \$13,500.00. The livestock notes were never restored to the accounts of the Western Bond & Mortgage Company.

The 1929 operation loss carried forward by the taxpayer has been reduced by the additional profit on the above deal.

In January of 1930 the Western Bond & Mortgage Company acquired the capital stock of the Consolidated Finance Co., of Washington and the capital stock of the Northwestern Finance Co. In February 1930 it sold these stocks to the Consolidated Credit Corporation for \$100,000.00. This sale showed a profit of \$70,000.00. Taxpayer did not include this profit in its taxable income but credited it to a suspense account on its books. The suspense account was not closed at the end of 1930. This profit has been added to taxable income in this report.

In October 1930 it was made to appear through a series of book entries that the Western Bond & Mortgage Company purchased from the Consolidated Credit Corporation the following assets:

87 Shares Preferred & 2500 Shares of Common stock of Consolidated Credit Company .....	\$320,000.00
250 Shares Common Stock Northwestern Finance Co. ....	50,000.00
250 Shares Common Stock Consolidated Finance Co. of Washington.....	60,000.00
500 Shares Common Stock Surety Fi- nance Co. of Vancouver.....	45,000.00
1843-2/3 Shares of Class "A" Common Stock of Consolidated Credit Cor- poration .....	35,429.65

Live Stock Notes Receivable.....	134,851.21
Accrued Interest on above.....	3,197.97

Then the Western Bond & Mortgage Company was supposed to have liquidated the Consolidated Credit Company, the Northwestern Finance Company, the Consolidated Finance Company of Washington and the Surety Finance Company of Vancouver, and to have sold back the assets of the Northwestern Finance Company and the Surety Finance Company of Vancouver to the Consolidated Credit Corporation. The net sales price at which the assets of these companies were transferred to the Consolidated Credit Corporation were:

Northwestern Finance Company.....	\$ 7,000.00
Surety Finance of Vancouver.....	44,324.22

Losses on the above transactions were claimed on the return.

When the Western Bond & Mortgage Company took over the 87 shares of Preferred and the 2,500 shares of common stock of The Consolidated Credit Company it already owned 413 shares of the preferred stock. This transfer gave it possession of all of the outstanding capital stock of the Consolidated Credit Company.

Prior to transferring this stock to the Western Bond & Mortgage Company the Consolidated Credit Corporation had taken over all of the assets and assumed all of the liabilities of the Consolidated Credit Company except a note receivable to the Western Bond & Mortgage Company amounting to \$300,000.00. When the Western Bond & Mortgage Company had all the stock of the Consolidated Credit Company the only asset remaining was its own note. Its books showed an investment in the stock of the Consolidated Credit Company of \$361,300.00 and the only asset it received was its own note for \$300,000.00. A loss of \$61,300.00 was claimed on this liquidation.

At the same time it appears on the books of the Western Bond & Mortgage Company that it purchased \$250,000.00 worth of the common stock and \$50,000.00 of the Preferred Stock of the Baldy Finance Company

and \$40,500.00 of the common stock of the Baldy Finance Agency. The assets of the Consolidated Finance Company of Washington, which the Western Bond & Mortgage Company had taken over in the supposed liquidation of the stock which had cost it \$60,000.00 were then transferred to the Baldy Finance Agency in payment for the \$40,500.00 worth of capital stock and a loss was claimed for the difference. The stock of the Baldy Finance Agency was then transferred to the Consolidated Credit Company for \$35,000.00 and a further loss was claimed on the transaction.

The \$250,000.00 worth of common stock of the Baldy Finance Company was then transferred to the Consolidated Credit Corporation for a purported price of \$562,500.00 or a profit of \$312,500.00.

After analyzing all of the above transactions it appears that the net result was a gain to the Western Bond & Mortgage Company, which gain has been returned as taxable income.

The Live-Stock Notes Receivable transferred in the above deals were the balances remaining on the \$300,000.00 worth of notes which had been transferred in 1929 by the Western Bond & Mortgage Company in payment of its stock subscription of 100,000 shares of Class "A" Common Stock of The Consolidated Credit Corporation. As explained above none of these notes were realized on by the Consolidated Credit Corporation and by a series of exchanges and substitutions were all transferred back to the Western Bond & Mortgage Company, the amounts transferred in the above deal being the final clean up. The Western Bond & Mortgage Company charged these balances off as worthless in 1930. The charge off has been disallowed for lack of proof that these notes actually became worthless in the year 1930.

During 1930 the Western Bond & Mortgage Company carried on a conversion campaign whereby it induced some of the holders of its installment bonds to convert these obligations into units of stock of the Consolidated Credit Corporation. The agreement between it and the bond-holders was that the bond-



holders would subscribe for sufficient units of stock of the Consolidated Credit Corporation at \$15.00 per unit to equal the maturity value of the bond, the bondholders would be given credit on their subscription for the full amount they had paid on the bond, and would be allowed to complete the payments upon the same basis on which they were paying out their bond. When payment was complete the stock was to be delivered but in the interim the Western Bond & Mortgage Company was to keep in trust sufficient units to equal the amounts which had been credited upon the subscriptions. The Western Bond and Mortgage Company had an agreement with the Consolidated Credit Corporation to purchase the units of stock at \$13.00 per unit, less 15% discount to be allowed for selling the stock. A unit of stock consisted of one share of preferred par value \$10.00 and one share of Class "A" Common with no par value which was sold to the Western Bond at \$3.00 per share and which was resold by it for \$5.00 per share. Both classes of stock carried the discount or commission for sale.

The amount of stock disposed of by the Western Bond & Mortgage Company under this conversion program amounted to \$1,531,520.70 and the collections and credits during 1930 amounted to \$578,375.55.

The Western Bond and Mortgage Company set up a profit on these conversions computed at \$3.95 per unit. It charged against this profit the commissions paid to salesmen, other expenses incurred in the conversion, and a reserve of \$84,585.85 for possible losses of profits on contracts which would not be completed. Experience showed that many of these contracts would not be completed and the policy has been where contracts were not completed to deliver units equal to the amount paid in and to cancel the balance due. Since it appears to be questionable as to whether many of these sales were actually completed transactions in 1930, and since the reserve for losses was transferred to another corporation in a deal described below, it would seem inadvisable to include this re-

serve in taxable income.

In 1930 the Western Bond and Mortgage Company was instrumental in forming a corporation known as the Western Guarantee Company. This company had an authorized capital stock of \$5,000.00.

The Western Bond & Mortgage Company transferred the following assets and liabilities to the Western Guarantee Company in exchange for the entire capital stock of the latter company.

Assets:

Accounts receivable for

stock sold \$1,531,520.70

Less: Payments and credits 578,375.55

---

Net	\$953,145.15
-----	--------------

Corporation Stocks Trusteed on stock sales	603,487.50
---	------------

Corporation Stocks Pledged on Notes Payable	187,220.00
--	------------

Corporation Stock Unpledged	40,008.50
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Total Assets	\$1,783,861.15
--------------	----------------

Liabilities:

Stock purchase liability	\$1,285,870.58
--------------------------	----------------

Note payable	161,478.00
--------------	------------

Accrued Interest payable	24,698.22
--------------------------	-----------

Reserve for possible losses	84,585.85
-----------------------------	-----------

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Total Liabilities	\$1,556,632.65
-------------------	----------------

Difference	\$ 227,228.50
------------	---------------

It will be noted that only accounts which had to do with the bond conversions were involved in the above transfer.

Since the above transfer comes with the provisions of Section 112 (b)-4 1928 Act no taxable income accrued on the above transfers.

At the time the Western Guarantee Company was formed practically all of the common stock of the Western Bond and Mortgage Company was owned either by C. H. Farrington or the Laurel Investment Company, a corporation controlled by Farrington.



Simultaneous with the formation of the Western Guarantee Company, Farrington made an exchange of all the common stock in the Western Bond & Mortgage Company owned by him and by the Laurel Investment Company with outside parties for certain securities. The understanding apparently being that, as soon as, the new stockholders came into control of the Western Bond & Mortgage Company they would cause that company to take the proper corporate action to trade the stock of the Western Guarantee Company to The Laurel Investment Company for the same securities previously traded to Farrington and Laurel Investment Company for the common stock of the Western Bond & Mortgage Company. The result of these trades was that the Laurel Investment Company was in possession of the stock of The Western Guarantee Company and the Western Bond and Mortgage Company had the securities previously traded to Farrington et al. for the common stock of the Western Bond and Mortgage Company.

The Western Bond and Mortgage Company took up the assets in trade at the face value and reported a profit on this deal of \$16,460.23. It appears that nothing would be gained by attacking the value used and this profit has been accepted as correct. The tax liability accruing to the Laurel Investment Company on this deal is being covered in a separate report on that company.

Some of the companies included in the consolidated return are merely shell companies the operations, if any, are merged with the transactions of the Parent Company and are included in its Profit and Loss. No separate schedules are shown for these companies.

#### Negligence Penalty:

Investigation showed the return to have been prepared in a careless and negligent manner without due regard to existing law and regulations and it is recommended that the five percent negligence penalty be asserted.

(Signed) L. C. GUNNING,  
Internal Revenue Agent.

**PLAINTIFF'S EXHIBIT NO. 60**  
**AMENDED REVENUE AGENT'S REPORT**

**COPY**  
**TREASURY DEPARTMENT**

office of  
 Commissioner of      Washington  
 Internal Revenue

May 7, 1943

refer to:  
 IT:R:E:Aj  
 JWH-9647

Collector of Internal Revenue,  
 Portland, Oregon

Attention: Bankruptcy Division.

In re: Western Bond and Mortgage Co.,  
 Portland, Oregon.

In accordance with your request of April 26, 1943, there is enclosed herewith a copy of the "revised" report of the internal revenue agent, dated January 13, 1933, which formed the basis for the assessment, against the above-named corporation, of a 1930 deficiency in income tax of \$40,772.61 and negligence penalty of \$2,038.63.

Should you require, in addition to the instant enclosure, a copy of the agent's "original" report, it is suggested that you obtain same from the internal revenue agent in charge, at Seattle, Washington, in order to obviate further delay, this office having experienced some difficulty in locating the file due to the present status of the case.

Timothy C. Mooney,

Deputy Commissioner,

By (signed) J. W. CARTER  
 Head of Division.

Enclosure:

Copy of "revised" agent's report.

11  
COPY

REVISED REPORT

In re: Western Bond & Mortgage Co.  
Preliminary Statement

<i>Summary</i>		
Year	Additional Tax	5% negligence penalty
1930	\$40,772.61	\$2,038.63

Net additional tax \$40,772.61      penalty \$2,038.63

As a result of protest filed and conference held in this office, a re-examination of the records in connection with the contentions set forth in the protest disclosed the following:

Gain on sale of stock in Consolidated Credit Company

The 1929 operating loss carried forward as a deduction on the original 1930 return was reduced by an additional profit on the sale of this stock of \$46,500.00. Taxpayer contends that this additional profit was taken up during 1929 and that the adjustment was in error. Examination of all of the book entries made in connection with this transaction indicates that all of the profit on this deal was taken up in 1929 by a series of book entries made at different times during 1929. The taxpayer's contention in connection with this item should be conceded and the 1929 operating loss to be carried forward to 1930 should be increased by the \$46,500.00 by which it was required in the original report.

Gain on sales of stock in Consolidated Finance Co.  
of Washington and Northwestern Finance Com-  
pany

An analysis of the suspense account in which the profits on the sales of these stocks was credited failed to disclose that these profits were closed into income during 1930 as contended by the taxpayer. No disclosure has been made of the detailed information by which it is contended it could be shown that this profit had found its way into 1930 income and it is recommended that no change be made in this adjustment.

## Bad Debts

The greater portion of the bad debt deduction disallowed was composed of a series of live stock loans of various ages which had been transferred to the Consolidated Credit Corporation in 1929 as part payment for a subscription of the capital stock of that company, and which had been re-transferred by that company to the taxpayer in exchange for other assets in 1930. Apparently, the Consolidated Credit Corporation never expected to, and in fact never did, collect on these notes, but merely used them as a medium of exchange until some other asset could be substituted. Nothing could be learned from the present officers or employees as to the dates of the loans, the nature thereof, the collateral security, or the steps taken to enforce collection. Due to lack of information, this deduction was disallowed. No further information is available at this time and it is recommended that no adjustment be made in this item.

## Income from installment bonds

No change was made in the original report on account of this item. The amount which the taxpayer included in income but which it now contends was included in error amounted to \$176,686.58 and was made up of two items under the captions of

Installment Bond Default Income	\$104,790.73
---------------------------------	--------------

Profit on bond conversions	71,895.85
----------------------------	-----------

Analysis of the transactions in connection with the conversion of the installment bonds disclosed that all of the above profit was derived from the conversion of the bonds and not from bonds in default as indicated by the taxpayer's protest.

During 1930, the Western Bond and Mortgage Company carried on an intensive campaign whereby it persuaded part of the owners of its installment bond obligations to convert these bonds into stock of the Consolidated Credit Corporation. The basis upon which this conversion was to be made was the allowance of the total amount paid in by the bondholder, plus interest, against the purchase of units of stock in the Consolidated Credit Corporation at \$15.00 per unit. A unit of stock consisted of one share of

preferred stock and one share of Class "A" Common stock. The Consolidated Credit Corporation was a separate company, but the taxpayer had an agreement with it for the purchase of these units of stock at \$13.00 per unit, the Western Bond & Mortgage Company to be allowed in addition 15% sales commission or \$1.95 per unit. Thus it can be seen that upon each unit disposed of, taxpayer realized a gain of \$2.00 plus commission of \$1.95 or \$3.95 per unit.

Part of the gain on these conversions was credited to profit on bond conversions account and the balance was credited to default income account. The \$104,790.73 closed into income from the Default Income Account was not in fact default income credited to this account in the regular course of business, but was profit realized on the sale of units of Consolidated Credit Corporation stock which had been erroneously credited to the default income account.

None of the so-called default income credited to this account in the regular course of business was transferred to Profit and Loss during 1930. A summary of the detailed accounts which go to make up the Installment Bond Liability Account as shown by the balance sheet is as follows:

Installment Bond A/cs	12/31/1929	12/31/1930
Cash surrender value	\$1,159,393.89	\$ 717,811.21
Contingent Liability	206,720.50	102,644.96
Contingent Surplus	361,772.72	174,608.42
Default Income	164,806.09	189,966.47
Interest Earnings	245,134.84	306,704.25
Misc. Conversion A/cs		8,127.94

Total per B/S	\$2,137,828.04	\$1,499,863.25
---------------	----------------	----------------

It may be seen from the above that even though the Cash Surrender Value and other Installment Bond Liability Accounts were substantially decreased; due to the conversions made in 1930, the Default Income and Interest Earnings Accounts were substantially increased.

There was a large number of bond conversions in 1930 and due to the confused state of the records, no



attempt was made to check each transaction.

The taxpayer has no proper ground for complaint against including the profit on these conversions in income and especially so when no change is made in its own computation and it is recommended that no change be made in this item.

#### Depreciation

The taxpayer makes certain claims for depreciation not taken on its original return as follows:

##### Western Bond & Mortgage Company

A claim is made for the allowance of depreciation on furniture and fixtures for both the years 1929 and 1930 in amount of \$1,831.06 per year. This depreciation is based on an average asset value of \$41,907.58 and a life of 10 years. Apparently, consideration has been given to assets, the cost of which has been previously recovered through depreciation charges. Reports for previous years disclose no information on depreciation. The books indicate a fixture and furniture account as follows:

12/31/1929	\$35,361.92
12/31/1930	35,603.87

The amount claimed of \$1,831.06 appears to be reasonable and to take into consideration, exhaustion and this amount is recommended for allowance for the years 1929 and 1930.

##### Western Insurance Agency

A claim is made for allowance of depreciation on Furniture & Fixtures for both these years, 1929 and 1930, in the amount of \$345.66. This deduction is based on an average asset value of \$3,456.63 and an average life of ten years. The furniture and fixture account per books shows the following:

12/31/1929	\$1,937.46
12/31/1930	1,937.46

Average	1,937.46
---------	----------

A ten percent rate on the above average cost equals \$193.75 per year and this amount is recommended for allowance for both the years 1929 and 1930.



### Broadway Oak Corporation

A claim is made for the allowance of depreciation on furniture and fixtures and on building for both the years 1929 and 1930 in the amount of \$3,465.41 per year.

No books and records could be located for this company, but inquiry into its affairs indicate that it disposed of these assets in the year 1929 to the Guarantee Trust Company of Portland, Oregon, and thereafter it was inactive.

The claim for depreciation for the year 1930 is in error as the taxpayer did not own the assets upon which it claims depreciation. Any allowance made for the year 1929 would merely increase or decrease the gain or loss on the disposition of the building and fixtures and would not alter the final result. It is recommended that no depreciation be allowed the Broadway Oak Corporation for either the year 1929 or 1930.

The revised figures which follow give effect to these recommendations.

# DEFENDANTS' EXHIBIT 62

IN THE DISTRICT COURT OF THE UNITED STATES, FOR THE DISTRICT OF OREGON.

JOHN BROCKIE,

Plaintiff,

vs.

WESTERN BOND & MORT-  
GAGE COMPANY, a corporation,  
C. H. FARRINGTON, E. F.  
O'FLYNN, W. E. JOHNSON,  
BEN WALLING, LAUREL IN-  
VESTMENT COMPANY, a cor-  
poration, WESTERN GUARAN-  
TY COMPANY, a corporation,  
BEACON INVESTMENT COM-  
PANY, a corporation,

Defendants.

E - 9189

COMPLAINT  
IN EQUITY

U. S. DISTRICT  
COURT

District of  
Oregon

Filed  
Mar. 13, 1931

Now comes the plaintiff, and for cause of suit herein against the defendants alleges:

## I.

\* \* \* \* \*

During all of the times herein mentioned defendant Laurel Investment Company was and now is a corporation duly organized, created and existing under and by virtue of the laws of the State of Oregon.

On or about December 1, 1930, defendant Western Guaranty Company was organized under the laws of the State of Oregon, and ever since was and now is a corporation duly created, organized and existing un-

der and by virtue of the laws of the State of Oregon.

\* \* \* \* \*

### III.

That during all of the times herein mentioned the defendant C. H. Harrington owned and controlled a majority of the capital stock, and completely controlled and dominated, the defendant Laurel Investment Company, and now owns a majority of the capital stock thereof and controls and dominates the affairs of said corporation. That for more than five (5) years last past the defendant C. H. Farrington and said Laurel Investment Company have owned and controlled a majority of the outstanding common stock, which has the exclusive voting power, of Western Bond & Mortgage Company, and through such ownership the said C. H. Farrington during all of said time, and up to about December 20, 1930, entirely controlled, dominated and directed the affairs and transactions of said Western Bond & Mortgage Company.

That the defendant C. H. Farrington caused the defendant Western Guaranty Company to be organized about December 1, 1930, the incorporators thereof being three persons then in the employ of Western Bond & Mortgage Company as clerks, and subject to the control and direction of the said C. H. Farrington, who then and for many years prior thereto was a director, President and general manager of said last named corporation. That when said corporation was organized substantially all of the capital stock thereof

was issued to Laurel Investment Company by direction of the defendant C. H. Farrington, and thereafter, and in the manner and for the purpose herein-after more fully set forth, the said capital stock was issued to Western Bond & Mortgage Company by direction of the said defendant C. H. Farrington in exchange for a large amount in value of the assets of the Western Bond & Mortgage Company.

That on or about December 1, 1930, the defendant C. H. Farrington caused the defendant Beacon Investment Company to be organized, the incorporators thereof being three employees of Western Bond & Mortgage Company, who acted under the direction of the said defendant Farrington. That after said corporation was organized, and by direction of the said defendant Farrington, all of the capital stock thereof was issued to Western Bond & Mortgage Company, and at the same time the said Farrington caused to be taken out of and transferred from the assets of Western Bond & Mortgage Company, a considerable sum in value to Beacon Investment Company.

#### IV.

Some time prior to December 20, 1930, defendants C. H. Farrington, W. E. Johnson, E. F. O'Flynn and Ben Walling entered into an agreement among themselves, and concerted and conspired together to engage in and consummate a series of transactions through which the defendant Farrington, directly and through Laurel Investment Company, should abstract,

obtain and appropriate to themselves, and without consideration, property and assets of Western Bond & Mortgage Company in the sum and value of upwards of Three Hundred Thousand (\$300,000.00) Dollars, and the defendants O'Flynn, Johnson and Walling should obtain control of a majority of the common stock of the Western Bond & Mortgage Company and thus a control of the affairs of said corporation. In execution of this agreement, concert and conspiracy, the defendant Farrington caused the Western Guaranty Company to be organized with a capital stock of Five Thousand (\$5,000.00) Dollars, which capital stock he caused to be issued to the Laurel Investment Company, which latter corporation, as heretofore alleged, was entirely controlled by him. Thereupon he caused the Western Bond & Mortgage Company, which also was entirely controlled by him through the stock ownership as hereinbefore alleged, to transfer to the Laurel Investment Company assets and property of Western Bond & Mortgage Company in the sum and value of upwards of Three Hundred Thousand (\$300,000.00) Dollars, in exchange for the capital stock of Western Guaranty Company, in exchange for the capital stock of Western Guaranty Company as hereinbefore stated. About the same time, and in consummation of the aforesaid agreement, concert and conspiracy, the defendants C. H. Farrington and Lurel Investment Company went through the form of agreeing to transfer unto the defendants O'Flynn, Walling and Johnson, or their



order, a majority of the common or voting stock of Western Bond & Mortgage Company, in consideration of the transfer unto the defendants Farrington and Laurel Investment Company of certain substantially worthless properties and securities which it was then agreed between said parties should be, in fact, and in the manner hereinafter described, taken over by the Western Bond & Mortgage Company in exchange for the stock of the Western Guaranty Company, thus enabling the defendant Farrington, directly and through the medium of said Laurel Investment Company, to obtain the properties and assets of the Western Bond & Mortgage Company in the sum or value of upwards of Three Hundred Thousand (\$300,000.00) Dollars which had been abstracted and appropriated from the stock of the Western Guaranty Company as hereinbefore set forth. Thereupon the defendants O'Flynn, Johnson and Walling went through the form of transferring or issuing unto the Laurel Investment Company and Farrington the following: (a) one Hundred (100) shares of no par value stock of Lake Lucerne, a Washington corporation, which corporation did not have at that time, and has not now, any substantial financial responsibility; and (b) Conditional sales contracts on automobiles, which were a number of old, defaulted and delinquent conditional sales contracts, which were worthless, as plaintiff is informed and believes and alleges the fact to be; and (c) A note in the sum of \$24,750.00 said to be secured by chattel mortgage executed by Ljung-



dahl Products Corporation of Tacoma to Massachusetts Mortgage Company, a Washington corporation, which note, as plaintiff is informed and believes and therefore alleges the fact to be, was uncollectible and of no substantial value; and (d) Note executed by W. J. Burwell to Massachusetts Mortgage Company for \$19,477.70, which note, as plaintiff is informed and believes and alleges the fact to be, was uncollectible and of no substantial value; and (e) Note of Massachusetts Mortgage Company to Laurel Investment Company dated December 20, 1930, for \$87,000.00.

The Massachusetts Mortgage Company, as stated, is a corporation organized and existing under and by virtue of the laws of the State of Washington, with its principal office in Seattle, and about a year or more ago the defendants O'Flynn and Walling obtained control thereof by acquiring a majority of the voting stock. That said corporation for some time has been in financial difficulties. That upon information and belief plaintiff avers that said note for \$87,000.00 was executed by Massachusetts Mortgage Company without consideration and without authority from its Board of Trustees, and that for these reasons, and further because of the doubtful financial condition of the said corporation, it is uncollectible. And upon information and belief the plaintiff further avers that all of the other properties hereinbefore described in subdivisions (a), (b), (c) and (d) of this paragraph, were the properties of Massachusetts

Mortgage Company, and the said transfers were made by the defendants O'Flynn and Walling for their own personal purposes and were without consideration to or authority from the Board of Directors of said corporation.

## V.

On or about the 20th day of December, 1930, and in furtherance of said agreement, concert and conspiracy, a meeting of the Board of Directors of Western Bond & Mortgage Company was held. Present at said meeting were the defendant C. H. Farrington, President and director of said corporation, and B. Lyle McCroskey, Secretary and director of said corporation. Thereupon the said Farrington and McCroskey, acting as directors, did elect the defendants Johnson and O'Flynn directors to fill two vacancies on the Board, and thereupon the said Farrington and McCroskey resigned as directors and as president and secretary, respectively, and thereupon E. J. Boxer, a business associate of the defendants Walling, Farrington and Johnson, and connected with the Ljungdahl Products Corporation aforesaid, was elected a director, and thereupon the defendant Johnson was elected President and the said O'Flynn was elected Secretary and Treasurer of the corporation. And thereupon, at the same meeting, the defendant Farrington, through the Laurel Investment Company, offered to exchange the various items of property described in subdivisions (a), (b), (c) and (e) of the preceding paragraph hereof, for all of the capital

stock of Western Guaranty Company, and this proposal was in form accepted by Western Bond & Mortgage Company by a vote of the defendants Johnson and O'Flynn. That this proposal was made and accepted in the manner aforesaid pursuant to the aforesaid agreement, concert and conspiracy, and to enable the defendant Farrington, directly and through the Laurel Investment Company, to obtain and appropriate properties of the Western Bond & Mortgage Company of the value of upwards of Three Hundred Thousand (\$300,000.00) Dollars, which had, as heretofore alleged, been abstracted and turned over to the Laurel Investment Company in exchange for the capital stock of Western Guaranty Company, and to enable the defendants O'Flynn, Johnson and Walling to obtain control of Western Bond & Mortgage Company through the use of the properties and assets of the Massachusetts Trust Company for that purpose in the manner herein set forth. That, as heretofore stated, the assets and properties so transferred by Laurel Investment to Western Bond & Mortgage Company in exchange for the capital stock of Western Guaranty Company were and are substantially worthless, which fact was at all times well known to the defendants Farrington, Laurel Investment Company, O'Flynn and Johnson and the said transactions were carried through with the intention and for the purpose of enabling the defendant Farrington to obtain upwards of Three Hundred Thousand (\$300,000.00) Dollars of the property of the Western Bond

& Mortgage Company without any substantial consideration therefor, and to enable the defendants Johnson, Walling and O'Flynn to obtain control of Western Bond & Mortgage Company without paying any substantial consideration therefor.

## VI.

That for upwards of five (5) years prior to the commencement of this suit the defendant Farrington, through the control of the Western Bond & Mortgage Company, has by numerous devices so managed and manipulated the business, transactions and affairs of said corporation, and sundry other corporations which he organized and controlled so as to impose many losses upon the Western Bond & Mortgage Company, and shift to it many questionable or worthless securities in exchange or by way of substitution for valuable properties and securities abstracted and taken over by the defendant Farrington, directly or through one of his numerous corporations. That during said time the defendant Farrington, directly or through sundry of the smaller corporations organized and controlled by him, as plaintiff is informed and believes, and therefore alleges the fact to be, has collected and retained very large sums as commissions upon loans made of the funds of the Western Bond & Mortgage Company, and large commissions upon insurance policies issued in connection with said loans, and has taken mortgages in the name of the Western Bond & Mortgage Company very much in excess of the sums loaned thereon, and has used and converted

the difference, directly or through sundry of his corporations; and has collected and used, directly and through sundry of his corporations, large sums by way of commissions and other charges in connection with the purchase and disposition of automobile paper with the funds of the Western Bond & Mortgage Company; and has at divers times substituted securities of little or no value which he had acquired, directly or through some of his sundry corporation, for securities of full value owned by the Western Bond & Mortgage Company, so that there would pass into the assets of Western Bond & Mortgage Company the said questionable, doubtful or worthless securities, and pass out from its assets securities of full and unquestioned value.

\* \* \* \* \*

### XIII.

\* \* \* \* \*

That it would be useless to make demand upon the defendants, Johnson, O'Flynn and Walling to seek to recover from the Laurel Investment Company and Farrington the capital stock of Western Guaranty Company or to recover for the Western Bond & Mortgage Company the assets taken out in exchange for the capital stock of Western Guaranty Company, for the reason that said transactions were initiated and consummated as the result of the agreement, concert and conspiracy to which the said Johnson, O'Flynn and Walling were parties, as hereinbefore alleged, and it would be necessary, in order for them to seek



any judicial redress in behalf of the corporation with respect to such transactions, to sue and to charge themselves with improper, wrongful and corrupt conduct with respect to such matters. And it would be equally futile and useless to seek corporate redress for the wrongs committed on the corporation by the defendant Farrington, directly and through his sundry corporations as hereinbefore alleged, through the defendants O'Flynn, Walling and Johnson, or through any suit or action controlled or directed by them, for the obvious reason that it would be necessary for them to sue Farrington, with whom they concerted and conspired as hereinbefore alleged.

\* \* \* \* \*

WHEREFORE, Plaintiff prays for the decree of this court as follows:

1. That the defendant C. H. Farrington be required to account for all commissions and all profits made by him, and all sums received by him, in connection with the business, transactions and affairs of the Western Bond & Mortgage Company, other than the salary to which he became entitled as an officer of said corporation and as fixed and authorized by the Board of Directors thereof, and for all moneys, assets and properties of every character taken from the said Western Bond & Mortgage Company and transferred either to the Laurel Investment Company, the Western Guaranty Company, the Beacon Investment Company, or any other of the sundry corporations controlled by the defendant C. H. Farrington;



2. That the defendant, Laurel Investment Company, be required to account for and to turn back to Western Bond & Mortgage Company all moneys, assets and properties of every character which it received in exchange for the capital stock of Western Guaranty Company, and all other moneys, assets and properties whatsoever which have been transferred to it by Western Bond & Mortgage Company;

3. That the defendant Beacon Investment Company be required to account for and turn back to Western Bond & Mortgage Company all moneys, properties and assets which it has received from or which have been transferred to it by Western Bond & Mortgage Company;

4. That the defendant Western Guaranty Company be required to account for and to turn back to Western Bond & Mortgage Company all moneys, assets and properties whatsoever which it has received from or which have been transferred to it by Western Bond & Mortgage Company;

5. That the defendants, and particularly the defendant C. H. Farrington, be required to account for all mortgages and other securities of value which have been taken from the assets of Western Bond & Mortgage Company, and mortgages and securities of less value substituted therefor;

6. That the defendants W. E. Johnson, E. F. O'Flynn and Ben Walling be required to account for and be held liable for the full value of all moneys,

assets and properties whatsoever belonging to Western Bond & Mortgage Company and which were by it transferred or delivered over to the defendants C. H. Farrington, Western Guaranty Company, Laurel Investment Company, Beacon Investment Company, or either thereof;

7. That full inquiry be made into, and an accounting had of all matters and transactions referred to in the complaint, and that the defendants, and particularly the defendant C. H. Farrington be held liable to Western Bond & Mortgage Company for all moneys, assets and properties whatsoever of the Western Bond & Mortgage Company lost, wasted or unlawfully appropriated or taken from the assets of Western Bond & Mortgage Company by reason of all the matters, things and transactions mentioned in the complaint;

8. That the defendants Western Bond & Mortgage Company and W. E. Johnson, E. F. O'Flynn, Ben Walling as officers and directors of Western Bond & Mortgage Company, be enjoined and restrained, pending the determination of this suit, from using, appropriating, transferring or otherwise disposing of any of the funds, assets and property whatsoever of Western Bond & Mortgage Company, and from withdrawing any mortgages or other securities from the Lawyers Title and Trust Company, or any other corporation, acting as trustee of any moneys, mortgages or other securities belonging to Western Bond &

Mortgage Company;

9. That a receiver be appointed for all of the choses in action, rights of action and suits whatsoever of Western Bond & Mortgage Company, to hold, manage and conserve the same until the determination of this suit, or in the alternative to take over and hold all of the properties and assets of said Western Bond & Mortgage Company, to prosecute all choses in action, rights of action and suits whatsoever, and to wind up the business affairs of said corporation;

10. For such other and further relief as to the court may seem just and equitable in the premises.

(s) CLARK & CLARK,  
Attorneys for Plaintiff.

UNITED STATES OF AMERICA	)	
	)	
District of Oregon	)	ss:
	)	
County of Multnomah	)	

I, JOHN BROCKIE, Being first duly sworn, depose and say that I am the plaintiff in the above entitled cause; and that the foregoing complaint is true, as I verily believe.

(s) JOHN BROCKIE.

Subscribed and sworn to before me this 9th day of March, 1931.

(s) VIVIAN FLEXNER,  
Notary Public for Oregon.

My Commission expires December 14, 1931.

## DEFENDANTS' EXHIBIT 63

(Excerpt from Article Appearing in Oregon Journal,  
Published in Portland, Oregon, March 31,  
1931 — Pg. 17, Column 6)

An order to show cause why a receiver should not be appointed for the Western Bond & Mortgage company and affiliated concerns was signed by Federal Judge McNary today after a complaint in equity had been filed by Colonel A. E. Calrk and Malcolm H. Clark, attorneys for John Brockie, plaintiff.

The complaint names as defendants, in addition to the Western Bond & Mortgage company, C. H. Farrington, president of the concern; E. F. O'Flynn, W. E. Johnson, Ben Walling, the Laurel Investment company, the Western Guaranty company and the Beacon Investment company.

The complaint involves more than \$800,000 for which the defendant is said to be liable, this amount being the total of installment bonds which are promissory notes of the defendant. These bonds or notes, it is claimed, were sold to the holders on the agreement and representation that they would be amply secured by real estate mortgages placed on deposit with a trustee.

There are also outstanding, in addition to the \$800,000, the complaint alleges, some \$12,000 or more of "participation certificates" in real estate mortgages, whereby the investors purchased an interest in mortgages or groups of mortgages. There are certificates of that character outstanding and unredeemed in the sum of \$51,000 it is alleged.

Other outstanding obligations against the firm are in excess of \$20,000, it is cited.

A complete account of all funds and salaries is asked in the suit which alleges that through various transfers of assets the creditors have been deprived of security for their investments in the firm.

**DEFENDANTS' EXHIBIT 64**

(Article Appearing in Portland Telegram—March 13, 1931—Pg. 1, Column 5)

Charges that C. H. Farrington, president and former director of the Western Bond & Mortgage company, through an intricate network of dummy-incorporated companies has recently abstracted more than \$300,000 worth of the assets of the former firm, are contained in a complaint filed in federal court Friday by John Brockie, Idaho stockman and stockholder in the mortgage company.

The complaint charges that for years past the Western Bond & Mortgage company has been insolvent, but that Farrington, by manipulation of worthless and questionable securities held, has concealed its condition from the stockholders and creditors of the firm.

Defendants named besides Farrington and the Western Bond & Mortgage company are E. F. O'Flynn, W. E. Johnson, Ben Walling, the Laurel Investment company, the Western Guaranty company and the Beacon Investment company. The suit was filed by A. E. Clark and Malcolm H. Clark, attorneys.

Brockie asks for a full accounting of the affairs of the Western Bond & Mortgage company and the appointment of a receiver; restitution by the Laurel Investment company, Beacon Investment company and Western Guaranty company of the Western Bond & Mortgage company of its securities, alleged to have been exchanged for worthless and questional securities, and an accounting by Farrington of all the commissions and profits taken from the firm aside from his salary, and of all the moneys and assets transferred from the Western Bond & Mortgage company to the other companies.



## DEFENDANTS' EXHIBIT 65

(Excerpt from Article Appearing in Oregonian, Published in Portland, Oregon, March 14, 1931—Pg. 2, Column 1)

Suit asking for a receivership for the Western Bond & Mortgage company and for an accounting of assets, securities and earnings of the company, and of its ex-president, C. H. Farrington, was filed in federal district court yesterday by John Brockie, an Idaho stockholder in the company, against Farrington, three of his business associates and three corporations he is alleged to have organized from time to time. Federal Judge McNary signed an order citing the defendants to show cause why a receiver should not be appointed.

The complaint charges Farrington with shifting assets and property of the Western Bond & Mortgage company, the Laurel Investment company, Western Guaranty company and Beacon Investment company from one to the other in such a manner that many securities which the complaint alleges are practically worthless were left in the hands of the Western Bond & Mortgage company, whereas the other corporations, of which Farrington was said to be organizer and principal owner, gained valuable securities.

Return to the Western Bond & Mortgage company of assets received in exchange for capital stock of the Laurel Investment company, Beacon Investment company and Western Guaranty company are asked in the suit. The suit also asks that a full inquiry be made into transactions specified in the complaint and that Farrington be held liable to the Western Bond & Mortgage company for all assets alleged to have been lost, wasted and unlawfully appropriated.

\* \* \* \* \*



# **DEFENDANTS' EXHIBIT 66**

IN THE DISTRICT COURT OF THE UNITED  
STATES FOR THE DISTRICT OF OREGON

JOHN BROCKIE,	)	No. E-9189
	)	
Plaintiff,	)	<b>ANSWER</b>
	)	
vs.	)	OF WESTERN
	)	BOND AND
WESTERN BOND & MORT-	)	MORTGAGE
GAGE COMPANY, a corporation,	)	COMPANY
C. H. FARRINGTON, E. F.	)	AND BEACON
O'FLYNN, W. E. JOHNSON,	)	INVESTMENT
BEN WALLING, LAUREL IN-	)	COMPANY
VESTMENT COMPANY, a cor-	)	
poration, WESTERN GUARAN-	)	U. S. District
TY COMPANY, a corporation,	)	Court
BEACON INVESTMENT COM-	)	District of
PANY, a corporation,	)	Oregon
	)	Filed
Defendants.	)	Mar. 23, 1941

Come now Western Bond and Mortgage Company and Beacon Investment Company, two of the above named defendants, and for their answer to the Complaint herein, admit, deny and allege as follows:

\* \* \* \* \*

## **III.**

Answering Paragraph III thereof, defendants deny that defendant C. H. Farrington owned and controlled a majority of the common stock and dominated Laurel Investment Company during all of the times mentioned in the Complaint, or at any time except from and after on or about November 1, 1930 when

he acquired such stock; deny that for more than five years C. H. Farrington and Laurel Investment Company owned and controlled a majority of the outstanding common stock of Western Bond and Mortgage Company, or any other or longer period than from on or about November 1, 1929, and up to December 20, 1930; deny that C. H. Farrington caused Western Guaranty Company to be organized; and deny that when organized its capital stock was issued to Laurel Investment Company; defendants allege that the directors of Western Bond and Mortgage Company caused said Western Guaranty Company to be organized on or about December 1, 1930, and that when it was organized its capital stock was issued to Western Bond and Mortgage Company in exchange for certain assets owned by the Western Bond and Mortgage Company.

\* \* \* \* \*

#### IV.

Answering Paragraph IV thereof, defendants, except as herein specifically admitted, deny each and every allegation in said paragraph and the whole thereof; and defendants specifically deny that the defendants C. H. Farrington, W. E. Johnson, E. F. O'Flynn and Ben Walling, or either or any of them prior to December 20, 1930, or at any other time, entered into an agreement, or any agreement and concerted and conspired to do or cause to be done or did any of the things, transactions or acts sets forth therein; and defendants specifically deny that the

properties mentioned in subdivisions (a), (b), (c), (d) and (e) thereof were then or are now worthless or of little value; and deny specifically that the said Massachusetts Mortgage Company was then or for a long time had been or is now in financial difficulties; deny specifically that said acts were done without authority of its Board of Directors; and Defendants specifically deny that plaintiff is now or was informed and believed any or all of the facts he has alleged in said paragraph.

Further answering said Paragraph, defendants alleges that on or about December 20, 1930, the Massachusetts Mortgage Company, a corporation and the Laurel Investment Company on or about December 20, 1930, entered into an agreement pursuant to the terms of which the defendant Laurel Investment Company agreed to sell and the Massachusetts Mortgage Company agreed to purchase 5,662 shares of the Common Capital Stock of defendant Western Bond and Mortgage Company, all of which stock it owned and possessed at that time, whether standing on the books of said Western Bond and Mortgage Company in its name or not, and in payment of which it was agreed by said corporations that the Massachusetts Mortgage Company should transfer or cause to be transferred to the Laurel Investment Company the following described property, to-wit:

- (a) 100 shares of the Capital stock of Lake Lucerne, a Washington corporation;
- (b) Conditional sales contracts on automobiles of

the value of \$22,661.03;

(c) A promissory note of the Ljungdahl Products Corporation, a Washington corporation, in the sum of \$24,750.00;

(d) A promissory note of W. J. Burwell to the Massachusetts Mortgage Company of \$19,477.70; and

(e) A promissory note of the Massachusetts Mortgage Company for the sum of \$87,000.00, which latter note it was then and there agreed, could be paid by a note in said sum of the Northwest Hotels and Realty Corporation, a Washington corporation, to be secured by a mortgage upon certain real property in the City of Tacoma, Washington; that all of said properties are the same properties described in Paragraph IV of the Complaint; that at said time said parties consummated said transaction and made the exchange thereof as agreed and as herein set forth, and the Massachusetts Mortgage Company thereupon became the owner of the said stock of the Western Bond and Mortgage Company; that all of said transactions were had and done pursuant to the authority of the Boards of Directors of said corporations, and that all of the said properties transferred by the Massachusetts Mortgage Company had a real and substantial value, to-wit, the sum of \$253,888.73.

## V.

Answering paragraph V. thereof, defendants except as herein specifically admitted, deny each and every allegation of said Paragraph and the whole thereof; and defendants specifically deny that any of

the transactions mentioned therein were in furtherance of said "agreement, concert or conspiracy" or any agreement, concert and conspiracy; and defendants specifically deny that the properties therein mentioned, and described in paragraph IV of the Complaint in subdivisions (a), (b), (c), (d) and (e) were or are worthless or substantially worthless; and defendants specifically deny that there was transferred or assigned or given to C. H. Farrington upwards of \$300,000.00 of the property of the Western Bond and Mortgage Company or any property whatsoever.

Defendants admit that the directors of the Western Bond and Mortgage Company held by December 20, 1930, the meeting of its Board of Directors in said paragraph mentioned, and admit that at said meeting W. E. Johnson, E. F. O'Flynn and E. J. Boxer were elected directors of said corporation, and that C. H. Farrington and V. Lyle McCroskey then resigned as directors thereof.

Further answering said paragraph, defendants allege that on or about December 20, 1930, after the transaction had between the Massachusetts Mortgage Company and the Laurel Investment Company, set forth in the preceding paragraph of the Answer, was consummated, and closed by the exchange of said properties, that a meeting of the directors of Western Bond and Mortgage Company was held, and that at said meeting W. E. Johnson, E. F. O'Flynn and E. J. Boxer were elected directors thereof to fill vacan-



cies then existing on said Board, and qualified to act as such directors; that C. H. Farrington and V. Lyle McCroskey resigned as directors of said corporation.

That thereupon the Western Bond and Mortgage Company, and the Laurel Investment Company entered into an agreement pursuant to the terms of which the Western Bond and Mortgage Company agreed to sell and transfer to the Laurel Investment Company, and it agreed to purchase from the Western Bond and Mortgage Company the capital stock of Western Guaranty Company it owned, consisting of 500 shares, and as payment for said capital stock the Laurel Investment Company agreed to transfer to the Western Bond and Mortgage Company, and it agreed to accept the following described property, to-wit:

(a) 100 shares of the Capital stock of Lake Lucerne, a Washington corporation;

(b) Conditional Sales Contracts on automobiles of the value of \$22,661.03;

(c) A promissory note of Ljungdahl Products Corporation, a Washington corporation in the sum of \$24,750.00;

(d) A promissory note of W. J. Burwell in the sum of \$19,477.70; and

(e) A promissory note of the Massachusetts Mortgage Company for the sum of \$87,000.00, which note it was then and there agreed could be paid by a note of the Northwest Hotels and Realty Corporation, a Washington corporation, for the sum of \$87,000.00,



which note was to be secured by a mortgage upon real property in the City of Tacoma, Washington;

That at said time the said parties, the Western Bond and Mortgage Company and the Laurel Investment Company, consummated said transaction and made the exchange of said properties as agreed upon, and as herein set forth, and the Western Bond and Mortgage Company became the owner of said properties described in subdivisions (a), (b), (c), (d) and (e) hereof, and at said time it transferred, or caused to be transferred to Laurel Investment Company, the said 500 shares of the capital stock of Western Guaranty Company; that the properties received in said transaction and herein described had a real and substantial value, to-wit; the sum of \$253,888.73; that the said shares of stock of Western Guaranty Company were valued at about the sum of \$227,228.50;

That all of said transactions between the Western Bond and Mortgage Company and Laurel Investment Company were had and done pursuant to the authority of the Boards of Directors of said corporation, and thereafter at the Annual Meeting of Stockholders of Western Bond and Mortgage Company the said transactions of its Board of Directors were duly ratified, confirmed and approved.

## VI.

Answering Paragraph VI thereof, defendants specifically deny each and every allegation contained therein.

## VII.

Answering Paragraph VII thereof, defendants deny that C. H. Farrington handled, juggled and manipulated the mortgages mentioned therein in such a way as to make it appear that they were not in default, or for the purpose of deceiving stockholders of the Western Bond and Mortgage Company, deny that C. H. Farrington caused the corporations therein named to be organized, and allege in connection therewith the corporations named therein, which were and are owned by the Western Bond and Mortgage Company, were formed and organized pursuant to the authority and direction of the directors of said company.

Deny that the Keystone Finance Company was organized to take possession of the lands in Crook County, but admit that said corporation some time after its organization did take title to said lands in Crook County and gave the Western Bond and Mortgage Company the mortgages therein described; deny that said mortgages are delinquent, and deny that said lands have a value of not more than \$70,000.00.

\* \* \* \* \*

Admit Western Bond and Mortgage Company carries on its books 100 shares of the capital stock of Lake Lucerne, a Washington corporation, in the sum of \$100,000.00; deny that the same has no substantial value; the defendants believe and therefore allege that the same has a value of \$100,000.00 or more.

Admit Western Bond and Mortgage Company

carries 150 shares of the capital stock of Western Insurance Company in the sum of \$15,000.00; deny that the same has no substantial value; defendants believe and therefore allege that the same has a value of \$15,000.00 or more.

## XI.

Answering Paragraph XI thereof, defendants admit that there are certain livestock loans carried on the books of the Western Bond and Mortgage Company, and that some of the same may be uncollectible.

Defendants deny that the miscellaneous notes in the total amount of \$154,204.00 are worthless or uncollectible and deny specifically that the said Massachusetts Mortgage Company note of \$87,000.00, the note of W. Burwell and the note of Ljungdahl Products Corporation or any of them are uncollectible.

Defendants believe and therefore allege that all of said notes are worth their full face value and further allege that said Massachusetts Mortgage Company note has been paid in the manner agreed upon as heretofore alleged, that payment thereof was made by a note of Northwest Hotels and Realty Corporation, a Washington corporation, for the sum of \$87,000.00 which note is secured by a mortgage upon a very valuable parcel of real property in Tacoma, Washington.

## XII.

Defendants admit that among the assets of Western Bond and Mortgage Company are carried livestock open accounts in the sum of \$67,096.53, but deny

that all of the same are uncollectible, and specifically deny that said accounts have been kept and maintained for the purpose of deceiving stockholders and creditors of said corporation and concealing the true condition thereof.

Defendants believe and therefore allege that upon return to normal conditions the greater part of said accounts will be paid.

\* \* \* \* \*

For a separate and distinct defense in point of law arising upon the face of the bill of complaint herein, defendants allege:

\* \* \* \* \*

WHEREFORE, these defendants pray judgment that plaintiff's bill of complaint be dismissed with costs to these defendants, and for such other and further relief that may be just and equitable in the premises.

(s) J. P. KAVANUGH AND OSCAR FURUSET

Attorneys for Defendants  
Western Bond and Mortgage Company  
Beacon Investment Company  
605 Title & Trust Bldg.  
Portland, Oregon.

## DEFENDANTS' EXHIBIT 67

IN THE DISTRICT COURT OF THE UNITED  
STATES FOR THE DISTRICT OF OREGON

JOHN BROCKIE,

Plaintiff,

vs.

WESTERN BOND & MORT-  
GAGE COMPANY, a corporation,  
C. H. FARRINGTON, E. F.  
O'FLYNN, W. E. JOHNSON,  
BEN WALLING, LAUREL IN-  
VESTMENT COMPANY, a cor-  
poration, WESTERN GUARAN-  
TY COMPANY, a corporation,  
BEACON INVESTMENT COM-  
PANY, a corporation,

Defendants.

No. E-9189

ANSWER  
OF C. H.  
FARRINGTON

U. S. District  
Court  
District of  
Oregon  
Filed  
April 1, 1931

For answer to the bill of complaint of plaintiff  
herein, defendant C. H. Farrington says:

## I.

Answering the first paragraph of the bill this de-  
fendant admits that Western Bond & Mortgage Com-  
pany, Western Guaranty Company and Beacon In-  
vestment Company are corporations, and were organ-  
ized as alleged in said paragraph; admits that Laurel  
Investment Company is a corporation, but alleges  
that it was incorporated on or about December 9,  
1929.



## III.

Answering Paragraph III this defendant denies that he owned or controlled the majority of the capital stock or controlled or dominated defendant Laurel Investment Company at all the times mentioned in the complaint, or at any time, except that he purchased all of the capital stock of Laurel Investment Company on the 15th day of October, 1930, and has ever since owned same and now owns same; denies that for more than five years last past he and Laurel Investment Company, or either or both of them, owned or controlled a majority of the outstanding common stock of Western Bond & Mortgage Company, and alleges that he and Laurel Investment Company first acquired a majority of the common stock of Western Bond & Mortgage Company on October 29, 1929, and continued to own such a majority of said common stock until December 20, 1930 since which time neither of said defendants has owned any of the common stock of said Western Bond & Mortgage Company; denies that he at any time controlled or dominated the affairs of Laurel Investment Company, or of Western Bond & Mortgage Company, and alleges that the control and domination of said corporations were at all times vested in their respective Boards of Directors.

This defendant denies that he caused defendant Western Guaranty Company to be organized and alleges that said corporation was caused to be organized by the directors of the Western Bond & Mortgage



Company; admits that it was organized about December 1, 1930, and that the incorporators were three employes of Western Bond & Mortgage Company; denies they were subject to his control or direction; admits that he was for many years and up to December 20, 1930 the President and a director of Western Bond & Mortgage Company; denies that the capital stock of the Western Guaranty Company was on its incorporation issued to defendant Laurel Investment Company by his direction, or otherwise; denies that said capital stock of Western Guaranty Company was later issued to Western Bond & Mortgage Company by his direction, or otherwise, or in exchange for a large amount or any amount in value of the assets of Western Bond & Mortgage Company, and alleges that upon the incorporation of Western Guaranty Company all of its capital stock was issued to Western Bond & Mortgage Company.

\* \* \* \* \*

#### IV.

Answering Paragraph IV of the bill of complaint this defendant denies each and every allegation therein, except as hereinafter admitted and specifically denies that he, W. E. Johnson, E. F. O'Flynn and Ben Walling, or any one or more of them, prior to December 20, 1930, or at any other time, entered into any agreement among themselves, or concerted or conspired together to do any of the acts, things or transactions set forth in said paragraph; denies that he ever entered into any agreement of any kind with the

said W. E. Johnson, E. F. O'Flynn and Ben Walling, or any one or more of them; denies that he ever concerted or conspired with any one or more of the other persons named in said paragraph, or any other person, partnership or corporation to abstract, obtain or appropriate without adequate consideration any property or assets of the Western Bond & Mortgage Company of the value of the sum of \$300,000.00, or any value, and either through Laurel Investment Company or in any other manner; denies that he entered into any agreement, arrangement, conspiracy or concert with defendants O'Flynn, Johnson and Walling, or any one or more of them, or any other person to the end that the defendants O'Flynn, Johnson and Walling, or any one or more of them, should obtain control of a majority or any of the common stock of Western Bond & Mortgage Company.

Denies that he caused the Western Guaranty Company to be organized in execution of any agreement, concert or conspiracy, or otherwise, or at all; admits that Western Guaranty Company was organized with a capital stock of \$5,000.00; denies that he caused the capital stock of Western Guaranty Company to be issued to Laurel Investment Company, and denies that said capital stock was in fact issued to Laurel Investment Company.

Denies that defendant Western Bond & Mortgage Company was at any time entirely controlled or controlled at all by him; denies that he caused Western

Bond & Mortgage Company to transfer to Laurel Investment Company assets and property of Western Bond & Mortgage Company in the sum and value of upwards of \$300,000.00, or any other sum or value, or at all.

Admits that he and Laurel Investment Company sold to Massachusetts Mortgage Company 5145 shares of the common stock of Western Bond & Mortgage Company, but denies that said transfer was in pursuance of of any agreement, concert or conspiracy with the defendants O'Flynn, Johnson and Walling, or any one or more of them, either for the purposes described in said paragraph, or any other purpose.

Admits that after he and Laurel Investment Company had sold said stock to Massachusetts Mortgage Company and he had resigned as an officer and director of Western Bond & Mortgage Company and the positions he had held were filled by the new owners of said common stock, that defendant Laurel Investment Company traded to Western Bond & Mortgage Company the assets referred to in Subdivisions (a), (b), (c), (d) and (e) of said Paragraph IV for all of the capital stock of Western Guaranty Company; denies that said assets listed in Subdivisions (a) (b), (c), (d) and (e) were then or are now worthless or of little value, and alleges that the value of said assets at the time of said transfer equalled or exceeded the value of all of the capital stock of Western Guaranty Company.

This defendant alleges that he is without knowledge as to the ownership of the capital stock of Massachusetts Mortgage Company; denies that the Massachusetts Mortgage Company is or has been for some or any time in financial difficulties; denies that the note of the Massachusetts Mortgage Company for \$87,000.00 was executed without consideration or without authority from its Board of Trustees; denies that said note is uncollectible; admits that the assets listed in said paragraphs as (a), (b), (c), (d) and (e) belonged to Massachusetts Mortgage Company prior to the sale by defendants C. H. Farrington and Laurel Investment Company for said shares of common stock of the Western Bond & Mortgage Company owned by them; denies that the transfers of said assets or any other transfers referred to in said paragraph were made by the defendants O'Flynn and Walling either for their own personal purposes or at all, and denies that any of said transfers were without consideration to or authority from the Board of Trustees of Massachusetts Mortgage Company.

Further answering said paragraph this defendant alleges that on or about December 20, 1930 he and Laurel Investment Company sold to Massachusetts Mortgage Company 5145 shares of the common capital stock of defendant Western Bond & Mortgage Company, and in payment therefor Massachusetts Mortgage Company transferred to Laurel Investment Company the following described property, to wit:

(a) 100 shares no par stock Lake Lucerne, a

Washington corporation, being all of the capital stock of said corporation.

(b) Conditional sales contracts on automobiles totaling in value \$22,661.03.

(c) Mortgage from Ljungdahl Products Corporation to Massachusetts Mortgage Company upon a leasehold of lands in Pierce County, Washington, the amount of unpaid principal being at the time \$24,750.00.

(d) Note from W. I. Burwell to Massachusetts Mortgage Company in the amount of \$19,477.70 and certain collateral securities listed therein.

(e) Note of Massachusetts Mortgage Company to Laurel Investment Company dated December 20, 1930 for \$87,000.00.

This defendant further alleges that said purchase of said stock of Western Bond & Mortgage Company and the transfer to Laurel Investment Company of the assets above referred to was authorized by the Board of Trustees of Massachusetts Mortgage Company.

## V.

For answer to Paragraph V of the bill of complaint this defendant admits that at a meeting of the Board of Directors of Western Bond & Mortgage Company held December 20, 1930, C. H. Farrington and V. Lyle McCroskey resigned as directors of said corporation and W. E. Johnson, E. F. O'Flynn and E. J. Boxer were elected directors of said corporation.



This defendant further admits that after his resignation and that of V. L. McCroskey and the election of their successors, that defendant Laurel Investment Company sold to Western Bond & Mortgage Company the assets listed in subdivision (a), (b), (c), (d) and (e) of the preceding paragraph of this answer, and that Western Bond & Mortgage Company purchased the same and paid therefor by transferring to Laurel Investment all of the capital stock of Western Guaranty Company.

This defendant denies that said change in the personnel of the Board of Directors of Western Bond & Mortgage Company, and said trade of assets for the capital stock of the Western Guaranty Company, or any one or more of said events or transactions were in pursuance of any conspiracy, agreement or consent as alleged in Paragraph V of the complaint, or otherwise.

This defendant denies that E. J. Boxer is or ever has been a business associate of this defendant, and is without knowledge as to whether he is or ever was a business associate of defendants Walling and Johnson, or either of them, or whether he is or ever was connected with the Ljungdahl Products Corporation.

This defendant denies that said transfer of said assets for said Western Guaranty Company stock was in pursuance of any conspiracy or other than in the usual course of business; denies that any properties of the Western Bond & Mortgage Company of



the value of \$300,000.00 or of any value whatever had been abstracted or turned over to Laurel Investment Company in exchange for the capital stock of Western Guaranty Company, or otherwise, or at all. Denies that the assets transferred by the Laurel Investment Company to Western Bond & Mortgage Company were or are substantially worthless, and alleges that said assets were and are of a value equal to or in excess of the value of the whole of the capital stock of Western Guaranty Company; denies that said transfer was made without substantial or adequate consideration to the Western Bond & Mortgage Company; denies that said transfers was made to give control of the Western Bond & Mortgage Company to Johnson, Walling and O'Flynn or any of them; this defendant further alleges that said transaction between Western Bond & Mortgage Company and Laurel Investment Company was authorized by the Boards of Directors of both said corporations, and that the same was later ratified and approved at the annual meeting of the stockholders of Western Bond & Mortgage Company.

## VI.

For answer to Paragraph VI of the bill of complaint this defendant denies each and every allegation therein, and denies that he controlled Western Bond & Mortgage Company for a period of five years prior to the commencement of this suit, or for any period; denies that he managed or manipulated the business and affairs of said corporation in any way, and al-

leges that said corporation was managed and controlled during all of said times by its Board of Directors.

Denies that he imposed or caused to be imposed any losses upon Western Bond & Mortgage Company; denies that he shifted to it many or any questions or worthless securities in exchange for valuable properties and securities taken over by him, or that he shifted any questionable or worthless securities or any securities at all to said corporation in exchange for assets of said corporation taken over by him, either through any other corporation or otherwise.

Denies that he either directly or through any other corporation, or at all collected large sums or any sums as commissions upon loans made of the funds of the Western Bond & Mortgage Company, or large or any commissions upon insurance policies issued in connection with the Western Bond & Mortgage Company's loans, or that he ever took any mortgage in the name of the Western Bond & Mortgage Company in excess of the amount loaned or that he directly or indirectly ever converted any part of any loan made by said corporation; denies that he ever directly or indirectly collected or used any commissions or charges in connection with the purchase and disposition of automobile paper with the funds of Western Bond & Mortgage Company, or at all; denies that he at any time or ever substituted any securities of little or no value owned by him or any

corporation in which he was interested for securities of greater value owned by Western Bond & Mortgage Company; denies that he ever, directly or indirectly, transferred any questionable, doubtful or worthless assets to Western Bond & Mortgage Company in exchange for assets of greater value.

Denies that plaintiff has been informed by any person that any of the accusations against the said Farrington contained in Paragraph VI of the bill of complaint are true, and denies that plaintiff believes all or any of said charges to be true; and alleges that this suit was instigated by persons other than plaintiff which persons had previously attempted unsuccessfully by threats, intimidation and coercion to force this defendant to purchase their holdings of stock of Western Bond & Mortgage Company.

## VII.

\* \* \* \* \*

Denies that Keystone Finance Company was organized to take title to lands in Crook County, Oregon, or that said corporation was organized at all by him; admits that Keystone Finance Company did take title to lands in Crook County and did execute and deliver to the Western Bond & Mortgage Company two mortgages totaling \$150,000.00 and that said mortgages were up to December 20, 1930 deposited as a part of the security for outstanding installment bonds; denies that the lands covered by said mortgages are worth not to exceed \$70,000.00, and

alleges that all of the capital stock of Keystone Finance Company has at all times been owned by Western Bond & Mortgage Company, and that the lands covered by said mortgages were at the time said mortgages were taken and are now of a value substantially in excess of the total of said mortgages.

\* \* \* \* \*

### IX.

For answer to Paragraph IX of the bill of complaint, this defendant denies that defendants O'Flynn, Johnson and Walling, or any one or more of them, ever came into or have been, or are in control of Western Bond & Mortgage Company; this defendant admits that at the time defendant Laurel Investment Company and Farrington sold their stock in the Western Bond & Mortgage Company to Massachusetts Mortgage Company the mortgages and securities now on deposit with Lawyers Title & Trust Company were on deposit with Portland Trust & Savings Bank, and that at some time after December 20, 1930 said mortgages and securities were transferred to Lawyers Title & Trust Company; denies that Lawyers Title & Trust Company has no financial responsibility or property of substantial value; alleges he is without knowledge as to the purpose of such transfer, but on information and belief alleges said transfer was made without any purpose of looting the said mortgages and securities; admits that the trust agreement under which said mortgages and securities were deposited with Portland Trust & Savings Bank and later with

Lawyers Title & Trust Company permits Western Bond & Mortgage Company to make substitutions of mortgages and securities; denies each and every other allegation of said paragraph.

## X.

\* \* \* \* \*

This defendant admits that Western Bond & Mortgage Company carries on its books at a value of \$321,500.00 fifty shares of the capital stock of Central Realty Company, being all of the capital stock of said corporation; denies that said stock is of little or no value; alleges that Central Realty Company is the owner of large assets, but this defendant is without knowledge as to the exact value thereof.

This defendant admits that Western Bond & Mortgage Company carries on its books at the sum of \$100,000.00 one hundred shares of the capital stock of Lake Lucerne, a Washington corporation, being all of the capital stock of said corporation; denies said stock has no substantial value, and on information and belief alleges it is worth the sum of \$100,000.00.

\* \* \* \* \*

## XI.

For answer to Paragraph XI, this defendant admits that there are certain livestock loans carried on the books of the Western Bond & Mortgage Company, and that some of the same may be uncollectible.

This defendant denies that the miscellaneous notes in the total amount of \$154,204.00 are worthless or



uncollectible, and denies specifically that the said Massachusetts Mortgage Company note of \$87,000.00, the note of W. I. Burwell, and the note of Ljungdahl Products Corporation, or any of them, are uncollectible.

This defendant believes and therefore alleges that all of said notes are worth their full face value, and further alleges that the said Massachusetts Mortgage Company note has been paid in the manner agreed upon, that payment thereof was made by a note of Northwest Hotels and Realty Corporation, a Washington corporation, for the sum of \$87,000.00 which note is secured by a mortgage upon a very valuable parcel of real property in Tacoma, Washington.

## XII.

For answer to Paragraph XII this defendant admits that among the assets of Western Bond & Mortgage Company are carried livestock open accounts in the sum of \$67,096.53, but deny that all of the same are uncollectible, and specifically denies that said accounts have been kept and maintained for the purpose of deceiving stockholders and creditors of said corporation and concealing the true condition thereof.

This defendant believes and therefore alleges that upon return to normal conditions the greater part of said accounts will be paid.

## XIII.

For answer to Paragraph XIII this defendant denies that Western Bond & Mortgage Company is



now or has been at all insolvent; denies that defendants Johnson, O'Flynn and Walling control a majority of the voting stock of said corporation, or that they own or control any substantial amount thereof; denies that defendant Ben Walling is a stockholder, director or officer of said corporation, or ever has been; denies that E. J. Boxer is a director of said corporation; denies that the defendants Laurel Investment Company and C. H. Farrington, or either of them, ever entered into any agreement, concert or conspiracy of any nature whatsoever, with defendants Johnson, O'Flynn and Walling, or either or any of them.

\* \* \* \* \*

WHEREFORE, this defendant prays that this suit be dismissed as to him and that he have and recover from plaintiff his costs and disbursements herein, and have such other relief as may to the court seem equitable.

(s) WILSON & REILLY,  
Attorneys for Defendant  
C. H. Farrington.

UNITED STATES OF AMERICA )  
DISTRICT OF OREGON ) SS

C. H. FARRINGTON, being first duly sworn, on his oath, depose and says: that he is one of the defendants in the within action, that he has read the foregoing Answer, knows the contents thereof, and that the same is true.

(s) C. H. FARRINGTON.

Subscribed and sworn to before me this 1 day of  
April, 1931.

(s) JOHN F. REILLY,

Notary Public for Oregon.

(SEAL)

My commission expires: Nov. 29, 1934.

**DEFENDANTS' EXHIBIT 69**  
**MEMORANDUM OPPOSING DISMISSAL**  
**OF BROCKIE SUIT**

IN THE DISTRICT COURT OF THE UNITED STATES  
 FOR THE DISTRICT OF OREGON

John Brockie,

Plaintiff,

vs.

Western Bond and Mortgage Company, a corporation; C. H. Farrington; E. F. O'Flynn; W. E. Johnson; Ben Walling; Laurel Investment Company, a corporation; Western Guaranty Co., a corporation; Beacon Investment Co.

Defendants,

Massachusetts Mortgage Company, a corporation  
 Intervenor,

Town of Halfway, a Municipal corporation of the State of Oregon; Town of Richland, a Municipal corporation of the State of Oregon; Carl M. Little; C. H. Pape; Edward C. Pape; H. L. Temple; Frank P. Ofner; Clyde Graham; Gordon Ramstead; John J. Egr and Larry M. Wooton,

Intervenors.

**MEMORANDUM OF DEFENDANTS LAUREL INVESTMENT COMPANY, WESTERN GUARANTY COMPANY and C. H. FARRINGTON OPPOSING MOTION OF PLAINTIFF TO DISMISS.**

Several months ago the plaintiff instituted this suit and in presenting it to the Court represented that it was an emergency matter involving interest that not only justified but required the appointment of a Receiver pendente lite to protect the assets and re-

sources of the Western Bond & Mortgage Company and asserting the urgent necessity for the protection of the assets of that corporation.

The bill charges a conspiracy between the present owners of that corporation and C. H. Farrington, its former President, and charges a dissipation of the assets of the mortgage company by Farrington, and a conspiracy between the parties at present controlling the corporation, and Farrington. The Court denied the application for a Receiver and invited an application by the plaintiff for a restraining order to protect the existing assets and particularly the securities lodged with the trustee.

The Court called attention to the congested condition of its docket and stated that prompt hearing and action in the matter would require reference of the cause to a master and stated that unless objection thereto be made it would appoint the standing master of the court to hear and report upon the cause. At that time the cause was not at issue and of course it could not be referred until issue was joined.

The case was promptly put at issue, and thereupon the plaintiff filed his written motion for reference of same to a master. The plaintiff objecting to the appointment of the standing master as not being acceptable to all parties represented by counsel for plaintiff, the Court appointed Homer D. Angell, Esquire, as master, conditioned no objection be interposed by any of the interested parties.

All interested parties were consulted and the appointment of Mr. Angell was concurred in without opposition or objection by any of the parties, and the cause referred to him for full hearing and report on the facts and law.

In view of the fact that the master was appointed upon the motion of the plaintiff with the concurrence of all other parties this amounted to an arbitration before an agreed arbitrator pursuant to special rule of the court.

Had the parties failed to concur in or challenge the reference thus suggested by the court "a showing that some exceptional condition requires it" would have been necessary under Equity Rule 59. See also *Simpkins Federal Practice*, Pages 834 and 835.

Thus, irrespective of whether the reference to a master originated with the Court or with the parties involved in the litigation, it was in fact a consent reference accomplished by the concurrence of all interested parties.

Having been made by special rule of court as distinguished from the general rules by which the practice of the court is covered, the submission thereupon became and was irrevocable.

In making this concluding statement we do not wish to be understood as waiving our contention that upon the equity rules, the record in this case and the authorities cited, plaintiff's motion to dismiss without

prejudice must be denied.

Respectfully submitted,

JOHN F. REILLY,

ROY F. SHIELDS and

ARTHUR C. SPENCER,

Attorneys for the three Defendants first herein named.

Dated July 30th, 1931.



## DEFENDANTS' EXHIBIT 71

IN THE DISTRICT COURT OF THE UNITED  
STATES FOR THE DISTRICT OF OREGON

JOHN BROCKIE,

Plaintiff,

vs.

WESTERN BOND & MORT- )  
GAGE COMPANY, a corporation, )  
C. H. FARRINGTON, E. F. )  
O'FLYNN, W. E. JOHNSON, )  
BEN WALLING, LAUREL IN- )  
VESTMENT COMPANY, a cor- )  
poration, WESTERN GUARAN- )  
TY COMPANY, a corporation, )  
BEACON INVESTMENT COM- )  
PANY, a corporation, )

Defendants. )

No. E 9189

ORDER  
DISMISSING  
SUIT

This matter is now before the court upon motion of the plaintiff for a dismissal, without prejudice, and it appearing that said motion should be granted, it is therefore

ORDERED that the complaint herein and this suit be and they are hereby dismissed, without prejudice, upon the payment by plaintiff of the statutory costs of defendants and witnesses, including the costs of reference and such reasonable fees to the Master in Chancery as may be determined by the court.

Dated at Portland, Oregon, this 18th day of August, 1931.

(s) JOHN H. McNARY,  
Judge.

**DEFENDANTS' EXHIBIT 75**

**(Article Appearing in Oregon Journal—July 14, 1931,**

**Pg. 9, Column 1)**

Nine bondholders and stockholders of the Western Bond & Mortgage company today filed suit in circuit court seeking appointment of a receiver on the charge that its assets have been misappropriated and that it is insolvent.

The plaintiffs are H. C. Thompson, M. V. Newton, N. S. Rogers, E. J. Reid, Mathew Reid, Mrs. Charles Bockler, Mary Hawley Kemp, E. F. Baird and J. P. Tamiesie. Defendants named in the complaint are the Western Bond & Mortgage company, E. F. O'Flynn, W. E. Johnson and Ben Walling, directors, and the Lawyers Title & Trust company.

The suit followed the filing of a suit Monday by the Western Bond & Mortgage company seeking \$250,000 damages from the Universal Bond & Mortgage corporation, Guy LaFollette, George A. Nichols, George M. McDowell, Frank Bramwell, Harry Swart and F. B. Pratt on the charge that the Universal corporation, and its president, LaFollette, had formed a conspiracy to wreck the Western company by soliciting bondholders to file suits.

The Western company has been engage in business for more than 15 years, according to the complaint filed by the nine plaintiffs. The complaint sets out that the company has outstanding upwards of \$800,000 in installment bonds, \$12,000 in participation certificates in real estate mortgages, \$51,000 in mortgage certificates, and \$400,000 in preferred stock.

For many years prior to December 20, 1930, it is alleged C. H. Farrington owned and controlled the majority of the common stock of the company, which has the voting power. It is charged

that Farrington completely dominated its affairs and for the purpose of juggling the assets and fraudulently concealing the true facts concerning the company's assets and liabilities, caused to be organized a number of other corporations, the stock in all of which was owned by Farrington and controlled by him through dummies and employes of his and of the Western company. These corporations were the Laurel Investment company, Western Guaranty company, Beacon Investment company, Keystone Finance company, Central Realty company, Livestock Loan company, National Investment company, Grande Ronde Livestock company and others.

The plaintiffs charge that O'Flynn, Johnson and Walling entered into a conspiracy with Farrington to engage in a series of fraudulent transactions through which Farrington directly and through his own controlled corporations should abstract and appropriate property and assets of the Western in a sum upwards of \$300,000, and that O'Flynn, Johnson and Walling should obtain control of the majority of common stock of the Western Company and thus control of its affairs.

In addition to appointment of a receiver, the court is asked to enjoin the defendants from disposing of any of the funds.

**DEFENDANTS' EXHIBIT 76**

**Article Appearing in the Oregonian—July 15, 1931,  
Pg. 13, Column 1)**

Appointment of a receiver for the Western Bond & Mortgage company was asked in a suit filed in circuit court here yesterday by nine holders of installment bonds and preferred stock issued by the company. Charges that the concern is insolvent and that assets have been juggled and misappropriated were made in the complaint.

Monday the Western Bond & Mortgage company filed suit against the Universal Bond & Mortgage company seeking \$250,000 damages, and charging that the Universal company had conspired to wreck the Western company and had persuaded bond and stockholders to seek a receivership.

The plaintiffs in yesterday's action are H. C. Thompson, M. V. Newton, N. S. Rogers, E. J. Reid, Mathew Reid, Mrs. Charles Bockler, Mary Hawley Kemp, E. F. Baird, and J. P. Tamaiesie. The defendants are the Western Bond & Mortgage company, E. F. O'Flynn, W. E. Johnson, Ben Walling and the Lawyers Title & Trust company.

For 15 years, the complaint said, the Western Bond & Mortgage company has been selling installment bonds, which are in effect promissory notes of the concern. Outstanding at the present time is upwards of \$800,000 in such bonds, \$12,000 in participating certificates, \$51,000 in mortgage certificates and \$400,000 in preferred stock, the plaintiffs alleged.

For many years C. H. Farrington owned and controlled a majority of the common capital stock, the only stock having any voting power, and until December 20, 1930, was president and managing director of the company, they set out.

Prior to December 20, 1930, it is charged, the

defendants, O'Flynn, Johnson and Walling entered into a conspiracy with Farrington to engage in a series of fraudulent transactions through which Farrington directly and through a number of corporations controlled by him, particularly the Laurel Investment Company, should appropriate property and assets of the Western company worth about \$300,000. The transactions by which Farrington obtained the assets of the company were in legal effect the unlawful payment of dividends from the capital assets of the concern on common stock of the corporation, while assets were not available to liquidate current obligations, the complaint said.

#### Subsidiary Concerns Formed.

Such transfers of capital stock were made, it is alleged, that about December 20 O'Flynn, Johnson and Walling acquired control of the company, by delivering to Farrington liquid and marketable assets of the concern valued at about \$300,000. Farrington resigned as president and V. Lyle McCroskey as secretary, and Johnson became president and O'Flynn secretary-treasurer, it was said.

For the purpose of juggling the assets and fraudulently concealing the true facts concerning the company, Farrington for a number of years, and particularly in the last two years, caused to be organized a number of corporations of which he owned the controlling interest, the complaint said. Among them were the Laurel Investment company, the Western Guaranty company, the Beacon Investment Company, the Keystone Finance company, the Central Realty company, the Livestock Loan company, the National Investment company, the Oak Service corporation, the Warm River Livestock company, and the Grande Ronde Livestock company.

#### Assets Value Questioned.

Also to conceal from the bondholders and preferred stockholders, it was charged, O'Flynn, Johnson and Walling, and before them, Farrington



ton and his employes, deliberately juggled the financial statements of the corporation to show book value assets to be greatly in excess of any real value. Stocks of various corporations were shown on the books to be worth more than \$300,000 in excess of actual value. Similarly, livestock notes were carried and mortgages on real estate, pledged with the Lawyers' Title & Trust company in the amount of approximately \$600,000, were in many cases secured by property having no market value equal to the face of the mortgage, it was claimed. Mortgages, valued in excess of \$92,000, have been pledged with the Boise City National bank, the complaint stated.

The corporation is wholly insolvent, it was charged, and there is due from Farrington a sum in excess of \$250,000 for which suit should be brought.

The complaint asked that a receiver be appointed with authority to prosecute all necessary suits to recover the assets for the corporation. An order enjoining the Western company and the other defendants from disposing of any funds or property and restraining the Lawyers' Title & Trust company from transferring or delivering any of the mortgages or securities to the Western company also was asked.



**DEFENDANTS' EXHIBIT 78**

**(Article Appearing in Oregon Journal—July 19, 1934,  
Page 19)**

Salem, July 19.—Charges of irregularity by officers of the Western Bond & Mortgage company of Portland, as contained in the audit report of the state corporation commissioner's office, were submitted today to Attorney General Van Winkle and the district attorney of Multnomah county by Charles H. Carey, corporation commissioner, for full investigation and recommendations for indictment and recovery of property in the interests of investors.

The report included indication of fraud in mortgage transactions with affiliated companies, and "disregard for the actual liability in withdrawal of securities," as well as the statement that the firm is "hopelessly insolvent at the present time."

Officials mentioned in the audit report against whom criticism was made include E. F. O'Flynn of Seattle, president and in control of the company; W. E. Johnson, former president from Montesano, who now is reported in Canada, and E. E. Edmunds, who was declared "used as a tool to enable the officers to get cash."

The company, capitalized at \$1,000,000, was organized April 20, 1911, as an Oregon corporation, and operated chiefly in Portland and the Puget Sound country in Washington. The firm sold securities between February, 1923, and January, 1926, all sold under a trust agreement. Since that time no application to sell has been made under the blue sky law, but the investigation of the company was ordered by Carey last March as a result of complaints and questions received at his office from bondholders.

The audit report, filed with Carey by Charles A. Goodwin, auditor for the corporation commis-

sioner, pointed out that installment bonds now payable have a matured value of \$28,845, and the cash on hand was only \$62.42. He declared these payments cannot be made in cash.

The audit further points out several specific instances of alleged irregular transactions. It declared the disbursement of \$5142 to O'Flynn "appears irregular," and that specific mortgages unlawfully converted totaling \$68,012, were "defrauding the bondholders."

Another specific charge was made in the reputed mishandling of \$20,000 by O'Flynn, Edmunds and Johnson and an additional \$11,000 disbursement to O'Flynn through means of affiliated corporations.

During the present time, although the firm was declared "hopelessly insolvent", the officers were collecting about \$200 a month from installment bondholders which the officers are drawing on, the report stated. The total amount of the alleged improper transactions could not be computed in the preliminary investigation, Goodwin stated.

C. H. Farrington of Portland was president of the firm when it was organized. He was succeeded by Johnson, who was replaced as head by O'Flynn in 1932. Miss E. E. Gallagher is vice president and Miss L. Thibodeaux is an employe of the firm, both declared used as "dummies in alleged affiliated corporations."

The matter of the criminal prosecution was referred to District Attorney Lotus L. Langley of Multnomah county, while the proposal to protect the interests of investors in the attempted recovery of these mortgages "irregularly transferred" was referred to the attorney general. The corporation department declared this was the first time the attempt to recover property for investors had been referred to the attorney general.

**DEFENDANTS' EXHIBIT 79**

(Article Appearing in the Oregonian, Friday, July 20,  
1934, Page 5)

SALEM, OR. July 19 (Special) — Investigation of the affairs of the Western Bond & Mortgage company of Portland today was turned over to the attorney-general of Oregon and the district attorney of Multnomah county by the state corporation commissioner because of evidences of irregularities found in the audit report of the commission.

Charges of embezzlement by the officers of the company were contained in the audit just completed by Charles A. Goodwin of the corporation department and submitted to Charles H. Carey, commissioner. Carey referred the matter immediately to Attorney-General I. H. Van Winkle for redress in the interests of the bondholders and to the district attorney of Multnomah county for criminal prosecution.

**Three Officials Named.**

The audit report included indications of fraud in mortgage transactions with affiliated companies and "disregard for the actual liability in withdrawals of securities," as well as the statement that the firm is "hopelessly insolvent at the present time."

Officials mentioned in the audit report against whom criticism was made include E. F. O'Flynn of Seattle, president and in control of the company; W. E. Johnson, ex-president from Montezano, who now is reported in Canada, and E. E. Edmunds, who was declared "used as a tool to enable the officers to obtain cash."

The company, capitalized at \$1,000,000, was organized April 20, 1911, as an Oregon corporation, and has been operating chiefly in Portland and the Puget sound country in Washington. The firm sold securities between February, 1923, and

January, 1926, all under a trust agreement. Since that time no application to sell has been made under the blue sky law, but the investigation of the company was ordered by Carey last March as a result of complaints and questions received at his office from bondholders.

The audit report pointed out that installment bonds now payable have a matured value of \$28,845, and the cash on hand was only \$62.42. He declared these "payments cannot be made in cash."

The audit further points out several specific instances of alleged irregular transactions. It declared that disbursement of \$5142 to O'Flynn "appears irregular" and that specific mortgages unlawfully converted totaling \$68,012 was "defrauding the bondholders."

Another specific charge was made in the "embezzlement of \$20,000 by O'Flynn, Edmunds and Johnson" and an additional \$11,000 disbursement to O'Flynn through means of affiliated corporations.

During the present time, although the firm was declared "hopelessly insolvent" the officers were collecting about \$200 a month from installment bonds which the officers were drawing upon. The total amount of the embezzlement, or the improper transactions could not be computed in the preliminary investigation, Goodwin stated.

C. H. Farrington of Portland was president of the firm when it was organized. He was succeeded by Johnson, who was replaced as head by O'Flynn in 1932. Miss E. E. Gallagher is vice-president and Miss L. Thibodeaux is an employe of the firm, both declared used as "dummies in alleged affiliated corporations."

#### Attorney-General Gets Case.

The matter of the criminal prosecution was referred to District Attorney Lotus L. Langley of Multnomah county, while the proposal to protect the interests of investors in the attempted recovery of these mortgages "irregularly trans-



ferred" was referred to the attorney-general.

The corporation department declared this was the first time the attempt to recover property for the investors was referred to the attorney-general.

In the letter of transmittal of the audit on the Western Bond & Mortgage company to the district attorney of Multnomah county, the corporation commissioner stated "you will find there are several instances where the criminal statutes have been violated and I hereby request you to prosecute those who appear guilty."

In the letter to the attorney-general Carey requested that he "institute such civil proceedings as you consider appropriate for the protection of the interest of the investors of that corporation."

Farrington, who was the first president of the company, now resides in Portland. The statute of limitations prevents criminal action, if any is found, against him, the corporation department declared, but civil action for the recovery of property could be brought against him in the event it is proven illegal transactions were made during his term of office.

**DEFENDANTS' EXHIBIT 80**

**(Article Appearing in Oregon Journal, Saturday,  
Aug. 4, 1934, Pg. 8, Column 8)**

Salem, Aug. 4. Appointment of a receiver for the Western Bond & Mortgage Co. was requested Thursday by Attorney General I. H. Van Winkle. The request was made in a petition filed with the United States district court in Portland.

August 13 was set as the date for a hearing on the petition, filed following a request by Charles H. Carey, corporation commissioner, that a thorough investigation into the affairs of the company be made by the district attorney of Multnomah county and the attorney general.

The petition alleges that the company is insolvent and is wrongfully withdrawing securities deposited with the trustee in bankruptcy for the purpose of protecting outstanding bonds. These securities, it is alleged, are entirely inadequate to protect bondholders.

The petition sets out that there are 758 owners of bonds of the company of whom are residents of Oregon and owners of bonds valued at \$389,403.68.

Intervention by the state was based on a recent audit by Charles A. Goodwin, deputy corporation commissioner, in which it was shown that present liabilities of the company on outstanding bonds are not less than \$613,000 and that securities of the company are not nearly sufficient to pay bonds now matured.

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**(Article Appearing in Oregon Journal, Monday, Aug.  
13, 1934, Pg. 3, Column 2)**

Argument on an order to show cause why a receiver should not be appointed for the Western Bond & Mortgage company was opened before



Federal Judge McNary today.

The hearing is on application of I. H. Van Winkle, attorney general for Oregon, and Ralph E. Moody, his assistant. The state corporation commissioner is made a joint applicant with Gottlieb Jossi, William E. Koenig and Louise McClintock, holders of the defendant's bonds.

Following argument, the court will either take the matter under advisement, appoint a receiver or deny the application. A similar application filed two years ago resulted in denial of a receiver for the company.

**DEFENDANTS' EXHIBIT 81**

**(Article Appearing in Oregon Journal, Aug. 14, 1934,  
Pg. 18, Column 1)**

George M. McBride has been named by Federal Judge McNary as receiver for the Western Bond & Mortgage company, Portland. The appointment was made on petition of I. H. Van Winkle, attorney general for Oregon, and his assistant, Ralph E. Moody. Joint petitioners were the state corporation commissioner, Gottlieb Jossi, William E. Koenig and Louise McClintock.

The appointment was made following hearing of a petition in intervention which has been pending since November 25, 1931, and the receiver is to serve pending adjudication of the case or its dismissal or appointment of a trustee. The creditors who joined in the matter are seeking to protect interests of stockholders, creditors and investors of the company, according to Moody.

Henry Clay Agnew, Seattle attorney, appeared as counsel for the firm and declared that appointment of a receiver for a corporation is equivalent to condemning a man without trial. He said the company is now being operated for \$200 a month which he declared is cheaper than any receiver could run it.

In making his decision, Judge McNary said he could not see what could hurt the company more than to have a bankruptcy proceeding pending against it for three years.

The attorney general based his petition on the grounds that the company has been transactions preferring certain bondholders; that it has withdrawn securities and substituted securities of less value; that funds of the company have been dissipated and that the corporation commissioner has been refused access to the books.

The petition declares that the total liabilities of the company are in excess of \$718,000 and that the face and book value of all securities deposited is not more than \$657,000.

**DEFENDANTS' EXHIBIT 82**

(Article Appearing in Oregonian, August 4, 1934,

Pg. 14, Column 4)

SALEM, Or. August 3 (Special). Appointment of a receiver for the Western Bond and Mortgage company was requested by Attorney-General Van Winkle in a petition filed in the United States district court in Portland today. Hearing on the petition was set for Monday, August 13.

The petition followed the action of Charles H. Carey, state corporation commissioner, who recently asked the attorney-general and district attorney of Multnomah county to conduct a thorough investigation of the company's affairs to determine whether there was any criminal or civil liability under the blue sky law. E. F. O'Flynn, is president of the company and E. E. Gallagher is secretary.

Records show that the company filed a petition of bankruptcy on November 25, 1931, and this is still pending in the courts.

The petition sets out that the alleged bankrupt company made application to the state corporation commissioner for a permit to transact business as a dealer in Oregon and to sell installment, coupon and single payment bonds in the amount of \$500,000. This permit was granted on February 27, 1923. Thereafter, on July 25, 1923, another application was filed for permission to sell these bonds in the amount of \$1,000,000. This application also received approval.

The dealers permit subsequently was canceled June 15, 1926, but according to the petition, the company continued to collect its installments. Up to that time, it was alleged that the company had issued and sold these bonds in an amount aggregating \$8,100,000, with total liability on the bonds so sold of \$270,000.

## DEFENDANTS' EXHIBIT 83

(Article Appearing in Oregonian, August 14, 1934,  
Pg. 4, Column 1)

A receiver for the Western Bond & Mortgage company of Portland was authorized yesterday by Federal Judge McNary following hearing of a petition in intervention filed by I. H. Van Winkle, attorney-general for Oregon, in the involuntary bankruptcy proceeding which has been pending since November 25, 1931. Judge McNary named George M. McBride, attorney, as receiver.

The receiver was appointed pending adjudication of the case, or its dismissal or appointment of a trustee. Creditors joined with the state in the petition of intervention "to protect the interests of the stockholders, creditors and investors of the company." Ralph E. Moody, assistant attorney-general for Oregon, represented the state at the hearing and Henry Clay Agnew, Seattle attorney, appeared as counsel for the Western Bond & Mortgage company.

Expense Declared Low.

"To appoint a receiver for a corporation is equivalent to condemning a man without a trial. The company is being run now at a cost of \$200 a month, which is cheaper than any receiver could run it," stated Mr. Agnew in behalf of the company.

"I do not know what could hurt your company much more than to have a bankruptcy proceeding pending against you for three years," the court replied.

The petition for appointment of a receiver to investigate affairs of the company was made by the attorney-general on the alleged grounds that the company had made transactions preferring certain bondholders, that it had withdrawn securities and substituted securities of less value or no securities at all, that the funds of the company

were being dissipated and that the corporation commissioner had been refused access to the books.

#### Firm Held Insolvent.

The total amount of liabilities of the Western Bond & Mortgage company for installment, single payment and coupon bonds now outstanding is in excess of \$718,000, according to the attorney-general's petition. "Face and book value of all securities deposited with the trustee does not exceed \$657,000, and is far in excess of any actual value of securities and the Western Bond & Mortgage company is absolutely insolvent," it alleges.

The company is "unable to pay even the \$28,000 due and unpaid on the fully matured bonds issued by it. In some instances where worthless mortgages were substituted by the bankrupt with the trustee for mortgages of value, the property so mortgaged has been since the substitution sold for non-payment of taxes and other public liens, and such substitute mortgages as a security are entirely worthless," the petition charges.

The Western Bond & Mortgage company has not sold a bond since 1930, Mr. Agnew stated. The actual liability of the company is \$450,000. The trust agreement provides for substitution of security, he declared, and only three substitutions were made after the bankruptcy proceeding was filed. All were made longer ago than 18 months, he stated. The corporation commissioner has had access to the books, he said.

**DEFENDANTS' EXHIBIT 84**

**(Article Appearing in Oregonian, August 19, 1931,  
Page 18, Column 3)**

Suit brought by John Brockie against the Western Bond & Mortgage company, C. H. Farrington, E. F. O'Flynn, Ben Walling, Laurel Investment company, Western Guaranty & Mortgage company and Beacon Investment company for an accounting and receivership was dismissed in federal district court yesterday by Judge McNary on a petition by the plaintiff.

Brockie, a stockholder, alleged that Farrington, as principal owner, had juggled the financial affairs of the group to further his own interests at the expense of stockholders.



**DEFENDANTS' EXHIBIT 85**

**(Article Appearing in Oregon Journal, Sept. 10, 1931,  
Pg. 22, Column 7)**

An accounting of assets and appointment of a receiver for Western Bond & Mortgage company are sought in an action filed Wednesday in circuit court by Edward Pape, C. H. Pape, Frank P. Ofner, Clyde Graham, Gordon Ramstead, H. L. Temple, John J. Egr, Larry M. Wooton, Carl M. Little, Helen P. Baker, Herman Lindseth, Ralph Hibbs, R. A. Chisholm, Lee Martin, Jung Sing, Duck Wong and Roy H. Mills.

The plaintiffs asked that the receiver take charge of all assets, moneys and deposits with the Lawyers Title & Trust company, which are stated to total about \$300,000.

The Lawyers Title & Trust company and W. E. Johnson, E. F. O'Flynn and E. J. Boxer, directors of the bond company, are co-defendants with the Western Bond & Mortgage company.

# DEFENDANTS' EXHIBIT 86

IN THE CIRCUIT COURT OF THE STATE OF  
OREGON FOR MULTNOMAH COUNTY

H. C. THOMPSON, et al,	)	No. 101-174
	)	
Plaintiffs,	)	AMENDED
	)	COMPLAINT
vs.	)	
	)	Office of County
WESTERN BOND & MORT-	)	Clerk
GAGE COMPANY, et al.,	)	Multnomah County,
	)	Oregon
Defendants.	)	Filed
	)	November 21, 1931

Comes now the plaintiffs and file this as and for their amended complaint herein, and for cause of suit against the defendants, allege:

\* \* \* \* \*

That during the last many years one C. H. Farrington has owned or controlled a majority of the common capital stock of said corporation, which said stock is the only stock having any voting power attached thereto as an incident of ownership and that the said C. H. Farrington has during all of said time and up to the 20th day of December, 1930, been the President, Managing Director and the head of said corporation, and through the common capital stock owned by himself and his employees, has completely dominated and controlled the affairs of said corporation; that for the purpose of juggling the assets of, and fraudulently concealing from the knowledge of

the stockholders and holders of the securities of said corporation and from the holders of its preferred stock, the true facts concerning its various assets and liabilities, the said C. H. Farrington has during the last several years, and particularly during the last three years, caused to be organized divers and sundry corporations, the stock in all of which corporations was owned by the said Farrington and/or controlled by him through dummies and through employees of his and of the Western Bond & Mortgage Company, which employees in the main have had and now have no financial standing nor any ability to respond in damages or to pay for liabilities incurred by said corporations wrongfully and in its behalf and for which purpose the plaintiffs allege that the said Farrington caused to be organized the following corporations, viz:

Laurel Investment Company  
 Western Guaranty Company  
 Beacon Investment Company  
 Keystone Finance Company  
 Central Realty Company of Oregon  
 Central Realty Company of Idaho  
 Livestock Loan Company  
 National Investment Company  
 Oak Service Corporation  
 Warm River Livestock Company  
 Grande Ronde Livestock Company  
 Oakley Realty Company  
 Bear Valley Livestock Company  
 Russell Land & Livestock Company  
 Sawtooth Livestock Company

and others of like kind and character, the officers and directors of which were employees of the said Farr-

ington and/or Western Bond & Mortgage Company, defendant, and had no financial interest in said corporations but acted as officers and directors only by way of dummies at the instance and request of the said Farrington and said Western Bond & Mortgage Company;

## VII.

That for more than five years last past the said C. H. Farrington, and the said Laurel Investment Company, owned, dominated and controlled by him as aforesaid, owned and controlled a majority of the outstanding common capital stock which had the exclusive voting power of the Western Bond & Mortgage Company, defendant corporation, and that through said ownership the said C. H. Farrington, up to about December 20, 1930, entirely controlled, dominated and directed the affairs and transactions of the said Western Bond & Mortgage Company; that on or about the 20th day of December, 1930, the defendant, Farrington, personally and by and through owned and controlled corporations hereinbefore referred to, and particularly through Laurel Investment Company, entered into a transfer of corporate stocks, whereby Massachusetts Mortgage Company, having its principal office and place of business in Seattle, Washington, secured the controlling interest in the common capital voting stock of Western Bond & Mortgage Company, and one W. E. Johnson was made President of Western Bond & Mortgage Company, and one E. F. O'Flynn was made secretary of Western

Bond & Mortgage Company; that the plaintiffs are unable to ascertain the names of other directors or stockholders in said Western Bond & Mortgage Company as of the date of the filing of this amended complaint, for the reason that although demand has been made upon W. E. Johnson, president of said corporation, for such information, the corporate records and minute books of said corporation, Western Bond & Mortgage Company, are kept in Seattle, Washington, and the plaintiffs have been denied access thereto, and on plaintiffs' demand, the said Johnson, President of said Western Bond & Mortgage Company, has refused to produce said records, notwithstanding the order of this court heretofore entered, directing the defendants to give an inspection of all books and document of defendants to plaintiffs; but each of said named directors are interested in and are officers of Massachusetts Mortgage Company, the principal stockholders of Western Bond & Mortgage Company;

#### VIII.

That the said E. F. O'Flynn is the President of Massachusetts Mortgage Company and is in fact the managing head of and dominates and controls the Western Bond & Mortgage Company;

#### IX.

That in truth and in fact the transaction through which the defendants, Johnson and O'Flynn, through the Massachusetts Mortgage Company, acquired said common voting stock in said Western Bond & Mort-



gage Company, were by the unlawful and fraudulent abstraction of the property and assets of the Western Bond & Mortgage Company, in the sum of upwards of \$300,000.00, and so that the said defendants O'Flynn and Johnson, through the Massachusetts Mortgage Company, should obtain control of the majority of the common capital stock of the Western Bond & Mortgage Company and thus control all the affairs of the said defendant, Western Bond & Mortgage Company, a corporation, and on or about December 20, 1930, the said defendants did so acquire control, not by virtue of payments made or delivery of any assets then owned by the said O'Flynn, Johnson, and/or Massachusetts Mortgage Company, but rather by delivery to the said Farrington and Laurel Investment Company of the liquid, more valuable and marketable assets of the Western Bond & Mortgage Company;

\* \* \* \* \*

## XI.

That for the purpose of concealing from the bondholders and preferred stockholders of said corporation its true financial condition, the defendants O'Flynn and Johnson, and prior to the time they were elected directors of said corporation, the said Farrington by himself and by and through his employees, dominated and controlled by him, have with intent to deceive the bondholders and preferred stockholders, so juggled the financial statements of said corporation and have so juggled the mortgages deposited



with the trustee to secure the said bond holders, so as to show book value assets in said mortgages and also in the general assets of said corporation, to be greatly in excess of any real value of said assets so owned and controlled by said corporation and so as to deceive and defraud the said bondholders in relation to securities pledged with the said trustee; that in this connection plaintiffs allege that many of the mortgages pretended to be lodged with the said trustee are not in truth and in fact mortgages but that the mortgages so lodged with the trustee have been foreclosed; that the said defendants have for the purpose of deceiving the bondholders as to the real securities held by said trustee for their account, made fictitious and false credits of interest alleged to have been paid on said mortgages so as to give the said mortgages an apparent standing and real value when in truth and in fact the interest has been defaulted on said mortgages and has not been paid by the makers of said mortgages and said makers have only received credit for the payment of interest by false and fraudulent book entries made by the Western Bond & Mortgage Company; that there is recited in the next succeeding paragraphs instances of such dealing.

\* \* \* \* \*

### XIII.

That there is carried in said trust account mortgages executed by Keystone Finance Company, in the principal sum of \$150,000.00, secured by lands in

Crook County, Oregon, known and commonly called the Russell Ranch, concerning which the appraisals carried in Western Bond & Mortgage Company's files, show the said land to have been valued by the former owner, Russell, in 1926, at \$120,000.00, and on which the highest appraised value disclosed by the defendant's own files, is \$150,000.00; that interest is badly in arrears on said mortgage, and in truth and in fact said mortgage was originally for \$60,000.00; that the original maker of said mortgage, being unable to pay the taxes against said premises, or the interest on said mortgage, deeded said property over to Keystone Finance Company, a subsidiary of Western Bond & Mortgage Company, and controlled by it, which in turn placed two mortgages on said premises, aggregating the \$150,000.00 aforementioned, and lodged the same with the trustee for the security of bondholders;

\* \* \* \* \*

#### XXIV.

That there is also carried, as an asset of said corporation, the stock of Central Realty Company, at \$321,500.00; that the said Central Realty Company is a subsidiary of Western Bond & Mortgage Company and that its officers and directors are the same as the officers and directors of the Western Bond & Mortgage Company and/or employees of said company, who have no financial responsibility, and that Central Realty Company has no other assets other than corporate stocks in Keystone Finance Company, Keystone Investment Company and other worthless sub-

sidiary companies of Western Bond & Mortgage Company, and lands hereinbefore referred to, which are already mortgages to Western Bond & Mortgage Company for more than 200% of the actual value of its holdings;

\* \* \* \* \*

## DEFENDANTS' EXHIBIT 87

IN THE CIRCUIT COURT OF THE STATE OF  
OREGON FOR MULTNOMAH COUNTY

H. C. THOMPSON, et al,	)	No. 101-174
	)	
Plaintiffs,	)	ORDER
	)	
vs.	)	(Stamped) October
	)	6, 1931
WESTERN BOND & MORT-	)	(Stamp is blurred for
GAGE COMPANY, et al.,	)	balance but is usual
	)	Multnomah County
Defendants.	)	filing stamp)

This matter came on for hearing before the undersigned, Judge of the above entitled court, on Thursday, the first day of October, 1931, on motion of plaintiffs for an order requiring the defendants, Western Bond & Mortgage Company and Lawyers' Title & Trust Company, to give plaintiffs an inspection and permission to take a copy of all books, documents or papers in their possession or under their control containing evidence of matters relating to the merits of the above styled suit. The court having heard the arguments of counsel, it is

ORDERED that the said motion be, and the same is hereby allowed and the said defendants, and each of them, are hereby ordered and directed to permit plaintiffs to make an inspection of all books, documents and papers in their or either of their possession or under their control, relating to the assets and lia-

bilities of the said defendant, Western Bond & Mortgage Company, and relating to the securities held by Lawyers' Title & Trust Company, to secure the bonds issued by Western Bond & Mortgage Company and held by plaintiffs, such examination to be made during reasonable business hours and with as little inconvenience as possible to the defendants, the plaintiffs in said examination and inspection to be represented by their attorney, Allen H. McCurtain, or a competent accountant of his selection, and the information so obtained to be used by the plaintiffs only in the prosecution of the above styled suit.

DATED at Portland, Oregon, this.....day of October, 1931.

(S) W. A. ECKWALL,  
Judge.



## DEFENDANTS' EXHIBIT 88

IN THE CIRCUIT COURT OF THE STATE OF  
OREGON FOR MULTNOMAH COUNTY

H. C. THOMPSON, et al,	)	No. 101-174
	)	
Plaintiffs,	)	AFFIDAVIT
	)	
vs.	)	Office of County
	)	Clerk
WESTERN BOND & MORT-	)	Multnomah County
GAGE COMPANY, et al.,	)	Filed
	)	November 21, 1931
Defendants.	)	
STATE OF OREGON	)	
	)	SS:
COUNTY OF MULTNOMAH	)	

I, Allen H. McCurtain, being first duly sworn, say that I am the attorney for the plaintiffs in the above entitled suit; that subsequent to the date on which the above styled court made an order permitting the plaintiffs to examine the books and accounts of the defendant, I employed one, Carlson, a competent auditor, to examine the books, accounts and records of the defendant, Western Bond & Mortgage Company and Lawyers Title & Trust Company; that the said auditor has submitted to me a report containing information found in the books and accounts of the defendant, Western Bond & Mortgage Company, from which I am of the opinion it is absolutely necessary for the preservation of the assets of the said defendant that a temporary receiver be appointed to take

charge of the assets of said corporation, and that the said defendant be restrained from further disposing of or encumbering such assets, and as attorney for plaintiff I have prepared amended complaint, which has been filed herein; that I believe the facts stated in said amended complaint are true and that it is in the interests of justice and for the protection of the bondholders and stockholders of defendant, Western Bond & Mortgage Company, that an immediate hearing be had on an order to show cause why such relief should not be granted plaintiffs, and I further say that at said hearing there will be tendered to the court proof in support of the allegations set forth in said amended complaint.

Further affiant sayeth not.

(S) ALLEN H. McCURTAIN.

Subscribed and sworn to before me this 21st day of November, 1931.

(S) IRENE JOHNSTON,

Notary Public for Oregon.

My Commission expires: Oct. 9, 1933.

(SEAL)

**DEFENDANTS' EXHIBIT 103 AND 103A**  
**Excerpts from Transcript in McBride v. Bank of**  
**California**

**Excerpts from Amended Petition for an Order Re-**  
**quiring Bank of California to Turn Over Property**  
**(Pages 18 to 29)**

**II.**

That at the time of filing of the said petition in bankruptcy against the said Western Bond & Mortgage Company, the said Western Bond & Mortgage Company was the owner of all the capital stock of the Keystone Finance Company, an Oregon corporation; that said Keystone Finance Corporation was operated and manipulated at all times by the said Western Bond & Mortgage Company as its adjunct, subsidiary and agent, and for the sole purpose of carrying out its designs and biddings; that all the officers and directors of the Keystone Finance Company were chosen by the said Western Bond & Mortgage Company from the said Western Bond & (16) Mortgage Company's office employees who had no financial interest or actual stock holdings in said Keystone Finance Company and who acted without discretion or will of their own and as mere puppets to carry out the wishes and commands of said Western Bond & Mortgage Company; that said Keystone Finance Company had no office or place of business of its own, kept no books, made no tax returns to the Government, federal or

state, and did no independent business of its own, but that its office and place of business was the office and place of business of the said Western Bond & Mortgage Company, which kept the said Keystone Finance Company's books and which made the said Keystone Finance Company's tax returns as a part of its own books and its own tax returns; that the officers and employees of the Keystone Finance Company were paid no salaries or other compensation by the said Keystone Finance Company, but whatever salaries said officers and employees received were paid by said Western Bond & Mortgage Company as a part of the regular salary and compensation for services to the said Western Bond & Mortgage Company; that said Keystone Finance Company was a mere corporate shell and had no actual existence for its own purposes, but existed solely as subsidiary, underling, agent and alter ego of said Western Bond & Mortgage Company; and that the corporate existence of said Keystone Finance Company was against public policy of, and in fraud of, the State of Oregon. That said Keystone Finance Company held title in its name to certain real property in the County of Crook, State of Oregon, hereinafter to be designated as the Russell Ranch, consisting of over 8000 acres of land and described as follows:

\*       \*       \*       \*       \*       \*       \*

but that said title was held at all times by it for and on behalf of the said Western Bond & Mortgage Company as agent, subsidiary and alter ego of said West-

ern Bond & Mortgage Company, and that before, at, and after the filing of the petition in bankruptcy, against said Western Bond & Mortgage Company, said Western Bond & Mortgage Company in truth and in fact owned and was in possession of the fee in said Russell Ranch, and owned and possessed said property."

\* \* \* \* \*

#### V.

That at the time of the filing of the petition in bankruptcy by virtue of its ownership of all the stock in the Keystone Finance Co. and by further reason of its ownership of said mortgages, securing notes of the Keystone Finance Co. aggregating \$150,000.00, the said Western Bond & Mortgage Company actually and in fact owned both the equitable and legal title in the said Russell Ranch.

\* \* \* \* \*

#### IX.

That said plan or arrangement, to which the said Bank of California, National Association, was a party, contemplated or provided that the mortgages upon said Russell Ranch, heretofore referred to in Paragraph III hereof, securing notes of the said Keystone Finance Co., aggregating \$150,000.00 held by the said Western Bond & Mortgage Company would be released and satisfied by the said Western Bond & Mortgage Company and that at or about the same time the said Keystone Finance Co. would transfer to a company to be formed and to be known as the



Ochoco Farms Corporation said Russell Ranch heretofore described in paragraph II hereof, thus giving to the said Ochoco Farms Corporation the fee simple title to the said Russell Ranch, theretofore held by the said Keystone Finance Co., unencumbered, however, by any mortgage lien whatsoever. That said plan or arrangement further contemplated or provided that the said Ochoco Farm Corporation should execute to the Massachusetts Mortgage Company, a Washington corporation which owned stock in and controlled the said Western Bond & Mortgage Company and the said Ochoco Farms Corporation, a first mortgage 20) upon said Russell Ranch heretofore referred to, securing notes aggregating \$55,960.00, payable to the said Massachusetts Mortgage Company. And said plan or arrangement further contemplated and provided that the said Massachusetts Mortgage Company would thereupon assign said notes, aggregating \$55,960.00 and said mortgage securing them to the said Bank of California, National Association. And said plan or arrangement further contemplated and provided that twenty bonds issued by Boundary County, Idaho, Drainage District No. 10, each of the face value of \$500.00, owned by said Western Bond & Mortgage Company at the time of the filing of the petition in Bankruptcy against it should be transferred to said Bank of California, National Association.

\* \* \* \* \*



State of Oregon

County of Multnomah—ss.

\* \* \* \* \*

I, Geo. M. McBride, being first duly sworn, depose and say: That I am the petitioner herein and Trustee in Bankruptcy of the above entitled estate and that the facts contained in the foregoing petition are true as I verily believe.

GEO. M. McBRIDE.

Subscribed and sworn to before me this 11th day of August, 1936.

S. A. McALLISTER,  
Notary Public for Oregon.

FINDINGS OF FACT AND CONCLUSIONS  
OF LAW  
(Pages 58 to 69)

The names of certain companies occur with frequency in this record, viz.: Western Bond & Mortgage Company, Keystone Finance Company, Massachusetts Mortgage Company, Ochoco Farms Company, Bank of California, and a parcel of real estate called Russell Ranch. For brevity these corporations and the ranch will be herein referred to, in the order named, as follows, Mortgage Co., Finance Co., Massachusetts Co., Ochoco Co., the Bank, and the Ranch.

The sum and substance of the transaction to be inquired into, as set up by the pleadings, is com-

pounded of the following occurrences :

On November 25, 1931, an involuntary petition was filed against the Mortgage Co. by creditors, and subsequent steps resulted in its adjudication as bankrupt on September 24, 1934. On said November 25th it appears that control of its capital stock was possessed by Massachusetts Co.; that the Mortgage Co. in turn owned all of the stock of the Finance Co., which, in turn, held title to a livestock ranch in Crook County, Oregon, commonly called the Russell Ranch. This ranch embraces some 8,000 acres in area. Both the Mortgage Co. and the Massachusetts Co. were going concerns which were, or had been, doing considerable business in the field of finance, but the Finance Co. was merely a subsidiary of the Mortgage Co.; it did no business, its officers were supernumeraries and servants of the Mortgage Co., subject to the direction and control of the latter officers, and it held title to the ranch as auxiliary of the Mortgage Co., and by its direction. Pursuant to its function as a holding concern it had, some time (50) previously, executed and delivered to the Mortgage Co. notes for the sum of \$150,000, secured by a mortgage upon the ranch, which securities were still owned and possessed by the Mortgage Co. on November 25, 1931. At the date aforesaid, the Mortgage Co. was indebted to the bank in a sum upward of \$100,000 secured by collateral pledged. On and prior to February 13, 1932, the Bank deemed the collateral held by it insufficient to liqui-

date this debt; whereupon, on that date and a few days subsequently, the following took place:

The Mortgage Co. caused to be formed the Ochoco Co. and the Finance Co. to transfer to it title to the ranch. The Mortgage Co. thereupon released of record its mortgage security. Ochoco Co. executed and delivered to Massachusetts Co. notes totalling \$55,957, the amount required to liquidate certain advances some time previously made to Massachusetts Co. by the Bank, together with the debt of the Mortgage Co. to the Bank, the aforesaid sum being arrived at after computing the probable liquidation of the collateral held. The Finance Co. accompanied the notes by a mortgage upon the ranch, which was then unencumbered, and the Massachusetts Co. then assigned these instruments to the Bank. All these documents were recorded in Crook County, Oregon, on March 2, 1932. Also, as part of these transactions, there was transferred by Mortgage Co. to the Bank twenty certain Idaho irrigation bonds of the face value of \$500 each, which were also property of the Mortgage Co.

\* \* \* \* \*

So far as I now perceive the foregoing covers all the questions involved in this matter. The Bank undoubtedly possessed not only constructive knowledge of the position of the Mortgage Co. on the date aforesaid, but, in addition, it had, or acquired, actual knowledge of what was about to be done in the ultimate by all these instruments. Beyond any question

it knew, or could have known, that the Mortgage Co. owned a \$150,000 mortgage (57) upon this ranch. It knew, in addition, that the title held by the Keystone Finance Co. was for the benefit of the Mortgage Co.; in fact it knew that the Mortgage Co. was the only individual who had any interest in the ranch. It knew, from the very nature of the instruments drawn, and necessary to be drawn, that it was about to take from the Mortgage Co. its security, and when all the papers mentioned in these proceedings were by it filed for record in Crook County, Oregon, that it thereupon had, in fact, supplanted the Mortgage Co. with security, covering its own loan, upon said ranch and that the Mortgage Co. had been deprived of its security. It carefully computed the value of the collateral held by it and took the mortgage for the balance then remaining due from the Mortgage Co. to it, plus the moneys which it had theretofore passed to the Massachusetts Co. In doing all this it well knew that the Mortgage Co. was being deprived of an asset which belonged to it on the date of the petition, at all times after the petition, and which now belongs to it, and it may, in my opinion, be required to restore such status quo.

For these reasons the finding and conclusion is that the Bank must by order be required in some manner to restore the asset attempted to be destroyed by the instruments filed in Crook County, Oregon, on March 2, 1932, described in the pleadings in this case, and an order to this effect may be settled on service

and notice.

Dated at Portland, Oregon, February 8, 1937.

A. M. CANNON

Referee in Bankruptcy

Filed February 8, 1937. A. M. Cannon, Referee in Bankruptcy—Oregon.

## FINDINGS OF FACT AND CONCLUSIONS OF LAW

(Pages 70 to 82)

\* \* \* \* \*

(3) That at the time of the filing of said petition in bankruptcy against the Western Bond & Mortgage Company, all the capital stock of the said Western Bond & Mortgage Company was owned by the Massachusetts Mortgage Company, a Washington corporation, and that the Western Bond & Mortgage Company was the owner of all the capital stock of the Keystone Finance Company, an Oregon corporation; that said Keystone Finance Company was operated and manipulated at all times by the said Western Bond & Mortgage Company as its adjunct, subsidiary and agent and for the sole purpose of carrying out its designs and biddings, and was a mere corporate shell and had no actual existence for its own puproses, but existed solely as a mere agent and alter ego of the said Western Bond & Mortgage Company. That the officers and directors of said three corporations and of the Ochoco Farms Corporation, hereinafter men-



tioned, were interlocking.

(4) That said Keystone Finance Company at the time of the filing of the petition in bankruptcy herein held title in its name to certain real property in the County of Crook, State of Oregon, known as the Russell Ranch, consisting of some eight thousand acres of land and described as follows: (60)

\* \* \* \* \*

but that said title was held at all times by it for and on behalf of the said Western Bond & Mortgage Company as agent, subsidiary and alter ego of said Western Bond & Mortgage Company.

(5) That at said time of the filing of the petition in bankruptcy herein, the said Western Bond & Mortgage Company was also the owner of two notes, one in the amount of \$77,500.00 and the other in the amount of \$72,500.00, executed in its favor by the said Keystone Finance Company and secured by first mortgages duly recorded upon said Russell Ranch in favor of said Western Bond & Mortgage Company, and that said mortgages were first mortgage liens upon said property.

\* \* \* \* \*

(9) That thereupon and after the filing of the petition in bankruptcy against the said Western Bond & Mortgage Company caused to be formed a corporation named the Ochoco Farms Corporation under the laws of the State of Oregon, and caused the Keystone Finance Company to transfer to said Ochoco Farms



Corporation title to the said Russell Ranch, and simultaneously therewith the Western Bond & Mortgage Company, without receiving any consideration therefor, released and satisfied the said mortgages which it held against said property, thus giving to the Ochoco Farms Corporation the fee simple title to the said Russell Ranch unencumbered by any mortgage liens whatsoever. That thereupon the Ochoco Farms Corporation executed and delivered to the Massachusetts Mortgage Company a first mortgage upon said Russell Ranch to secure notes aggregating \$55,960.00, thereby supplanting the first mortgages theretofore held by the Western Bond & Mortgage Company. That the said Massachusetts Mortgage Company thereupon simultaneously assigned said notes, (62) aggregating \$55,960.00, and the mortgage securing the same to the Bank of California, National Association.

\* \* \* \* \*

(16) That the Bank of California, National Association, (64) had actual knowledge, prior to the receipt of the notes aggregating \$55,960.00 and prior to the assignment of mortgage to it securing said notes and prior to the executing and recordation of the instruments referred to in Finding No. 12, of the filing of the petition in bankruptcy against the Western Bond & Mortgage Company, and had actual knowledge at and prior to said time of the ownership by the Western Bond & Mortgage Company of the notes given by the Keystone Finance Company in the

amount of \$77,500.00 and of \$72,500.00, and of the ownership of the two first lien mortgages upon the said Russell Ranch to secure the payment of said notes, and of the recordation thereof; and that said Bank, also at said time, had knowledge of the fact that the recordation of the satisfaction of the mortgages held by the Western Bond & Mortgage Company and the recordation of the mortgage to the Massachusetts Company and the recordation of the assignment of that mortgage to it would supplant in its favor the first mortgage lien held by the said Western Bond & Mortgage Company upon said Russell Ranch, and accordingly would deprive the Western Bond & Mortgage Company of its property rights in said Ranch; and that the said Bank also had actual knowledge of the true character of the Keystone Finance Company in relation to the said Western Bond & Mortgage Company as set forth in Finding No. 3; and of the ownership by the Massachusetts Mortgage Company of all of the stock in the Western Bond & Mortgage Company, and of the interlocking character of the officers of the various companies, as also set forth in Findings No. 3.

\* \* \* \* \*

OPINION—NOVEMBER 17, 1941

(Pages 188 to 213)

James Alger Fee, District Judge:

The present controversy arises (1) on review of the Report of Referee on determination of order to

be made for restitution of real property to trustee and (2) on motion for re-hearing of the question of whether summary jurisdiction to order turnover was properly exercised.

\* \* \* \* \*

The development of the action commenced in the year 1929. Title to the "Russell Ranch" was then held by Western in the name of the Russell Company as wholly owned subsidiary which was actually operating the property. During that year Keystone was organized. On December 20, 1929, Russell Company deeded the "Russell Ranch" to Keystone. There was apparently no consideration for the transfer, as the value of the stock of the Russell Company from then on is carried as "nominal". On December 20, 1929, Keystone, through E. Hagenbucher, President, and L. Kelly, Secretary, executed two mortgages upon the "Russell Ranch" to Western. One of these was in the sum of \$72,500 and the other in the sum of \$77,500. Both were recorded December 28, 1929. On December 24, 1929, Keystone had increased its capitalization from \$1000 to 1500 no par value shares, obviously for the purpose of putting a fair face on the over-capitalization of the "Russell Ranch" above outlined. On January 6, 1930, Keystone had on deposit \$150,000, resulting from deposits of \$72,500 and \$77,500. On that date there was withdrawn \$72,500. It received \$27,600 on January 10th and \$45,000 on January 13th, and on January 21, 1930, the account was closed.

December 20, 1930, the Massachusetts Bond & Mortgage Company acquired complete control of Western common stock by sale from Laurel Investment Co. of 5146 shares thereof. As part of the purchase price, Massachusetts agreed to pay the obligations of \$112,537.57 of Western to the Bank at the rate of \$10,000 every six months until paid. On January 12, 1931, W. E. Johnson, E. F. O'Flynn and E. J. Boxer were elected Directors of Western, Johnson and O'Flynn only attending the meeting, and 5146 shares only being voted, O'Flynn voting 5044 as proxy of Massachusetts. In 1932 W. E. Johnson acted as President, E. E. Gallagher acted as Vice-President and E. F. O'Flynn as Secretary of the corporation. On January 12, 1931, there were issued to E. E. Gallagher, D. G. Smith and B. O'Reilly, respectively, 1 share of stock of Keystone and to Western the balance thereof in the amount of 1497.

\* \* \* \* \*

At the date of the bankruptcy, Western owned the Drainage District Bonds which it transferred or caused to be transferred to the Bank as a part of the transaction hereinafter set out. On February 11, 1932, a resolution was passed by Keystone to accept an offer of Ochoco (the articles of incorporation for which were not filed until February 16, 1932) of 850 shares of preferred capital stock of Western for the "Russell Ranch". This resolution is signed by E. E. Gallagher as President and L. Thibodeaux as Secretary of Keystone. The deed, pursuant to this resolu-

tion, was executed February 13, 1932, but not placed of record until March 2, 1932. On February 13, 1932, Western executed satisfaction of mortgages given by Keystone to it, dated December 20, 1929, in the sum of \$77,500 and \$72,500. These are signed by E. E. Gallagher, Vice-President, and attested by E. F. O'Flynn, Secretary-Treasurer, sealed with the corporate seal and acknowledged by both officers before Louise M. Thibodeaux as Notary Public.

\* \* \* \* \*

A review of the complicated facts indicates that Western owned the "Russell Ranch" but held title first in the name of Russell Company, from whence title was transferred at discretion of Western to Keystone, which, thereupon, mortgaged the land for more than its value to Western. Although the full amount of consideration for these mortgages was paid by Western to Keystone, this money disappeared from the Keystone account in a short time.

The question here, then, is how this particular real estate was held. The court held, heretofore, that although the record title was in the Keystone, actual title was in bankrupt.

\* \* \* \* \*

TESTIMONY TAKEN ON NOVEMBER 9 AND 10,  
1936, ON ORDER TO SHOW CAUSE TO BANK  
OF CALIFORNIA

(Page 249)

On November 9, 1936, at ten o'clock in the forenoon, the above entitled cause came on for hearing



before Honorable Anderson M. Cannon, Referee in Bankruptcy, upon an order to show cause directed to the Bank of California.

The Trustee in Bankruptcy, Mr. George McBride, was present and represented by his attorney, Mr. Sidney Teiser.

The Respondent, Bank of California, N. A. was represented by Mr. W. Lair Thompson of McCamant, Thompson & King.

\* \* \* \* \*

## TESTIMONY OF THOMAS G. GREENE

(Page 253)

Mr. Teiser. Before you answer may I ask whether you have produced the abstract of title requested?  
A. Yes.

\* \* \* \* \*

## Redirect Examination

(Page 256)

By Mr. Teiser:

Q. Mr. Greene, when you examined this title—you did examine the title, did you not?

A. I examined the title.

Q. As to the Russell Ranch? A. Yes.

Q. I may be a little ahead of my story. The (Testimony of Thomas G. Greene.)

Bank of California was receiving or taking assignment of mortgage from the Massachusetts Mortgage Company, the mortgage which had been given to them



by the Ochoco Farms Corporation?

A. It had not at the time I examined the abstract. It was merely discussed by the parties, the Bank of California, Mr. O'Flynn and myself. The abstract was brought to me first in the early (8) part of January, 1932.

Q. Before the assignment was taken you had the abstract before you. A. Yes.

Q. And at that time, I call your attention to page ten of these pages here, there appears to be recitation of the fact that the Keystone Finance Company, an Oregon corporation, had executed a mortgage to the Western Bond and Mortgage Company for seventy-two thousand five hundred dollars, executed on the 20th day of December, 1929; and another mortgage from the Keystone Finance Company, an Oregon corporation, to the Western Bond and Mortgage Company for seventy-seven thousand five hundred dollars, making a total of the two mortgages, and the notes secured by the mortgages, of a hundred and fifty thousand dollars?

A. That is correct.

Q. And that was apparent in the abstract?

A. It was. Let me see that page there.

\* \* \* \* \*

(Page 259)

Q. The abstract also shows a deed from the Keystone Finance Company, an Oregon corporation to the Ochoco Farms Corporation, dated February 13th

and recorded March 2, 1932, of the property covered by the mortgages and the satisfactions of mortgage; is that right?

A. Yes, if it is there. I did not charge my memory as to what was in the abstract.

Q. That is the reason I am calling your attention to it. A. That is what it shows.

\* \* \* \* \*

### TESTIMONY OF E. E. GALLAGHER

(Page 269)

Mr. Teiser. I merely wanted to show that the Western Bond and Mortgage Company was owned and controlled by the Massachusetts Mortgage Company.

Mr. Thompson. We will admit it.

\* \* \* \* \*

(Page 277)

Q. I hand you affiliations schedule of income tax return for 1930 of the Western Bond and Mortgage Company and ask you whether or not the signatures attached thereto of W. E. Johnson and E. F. O'Flynn attached are the signatures of these people who were officers of the Western Bond and Mortgage Company?

A. Yes. I recognize the signatures of Mr. Johnson and Mr. O'Flynn. (29) (Testimony of Miss E. E. Gallagher.)

Q. Were they directors of the Western Bond and Mortgage Company? A. Yes, they were.

Mr. Teiser. I offer this schedule in evidence with

the papers attached to it and call particular attention to the item "7" on the schedule and to item "10", one showing the ownership of all the stock in the Central Realty Company by the Western Bond and Mortgage Company, and the other showing stock of the Keystone Finance Company owned by the Western Bond and Mortgage Company.

Mr. Thompson. Object to it as something we could not possibly have had knowledge of at the time, and it cannot be binding upon us, and it don't prove ownership of the stock; anyhow it is incompetent and immaterial.

Mr. Teiser. That is the statement of the Western Bond and Mortgage Company signed by its officers and shows they made oath that they owned five shares of stock in the Central Realty Company and the entire ownership of the Keystone.

\* \* \* \* \*

(Page 301)

Mr. Thompson. It is a self-serving statement and cannot be binding.

The Court. It can go in under the objection.

Mr. Thompson. Is it necessary to save exceptions; may that be understood that we save exceptions to the ruling?

The Court. That may be understood.

The papers were marked Trustee's Exhibit 7, Nov. 9, 1936. (30)

\* \* \* \* \*

Q. I will ask you whether or not Mr. O'Flynn on the 20th day of December, 1930, was not elected a director of the company? A. Yes.

Q. And ask you whether or not Mr. Johnson was elected president at the meeting of December 20, 1930 and Mr. O'Flynn was elected secretary-treasurer on that date? A. Yes.

(Testimony of Miss E. E. Gallagher.)

Q. And that they continued as president and secretary-treasurer and director respectively until the 2nd day of May, 1932; is that right? A. Yes.

Q. Where was the office of the Keystone Finance Company in February, 1932?

A. At the Western Bond and Mortgage Company.

Q. And for a time previous to that was it there? (55)

A. You mean how far back was it there?

A. It was there for some time previous to that time? A. Yes.

Q. Did the Keystone Finance Company pay any rent for its offices during that period of time?

A. Not as far as I know.

Q. You were president, were you not?

A. Yes.

Q. Were you or any of the other officers of that company paid any salary as officer of that company by the Keystone Finance Company? A. Yes.

Q. Your entire compensation came from the Western Bond and Mortgage Company?

A. You mean our salary?

Q. Yes. A. Yes.

Q. In other words you received no compensation from the Keystone Finance Company?

A. No.

Q. Nor did any of the other officers so far as you know? A. So far as I know.

(Testimony of Miss E. E. Gallagher.)

Q. You were president and a director?

A. Yes.

Q. Were you and Miss Smith and Miss O'Reilly employees of the Western Bond and Mortgage Company? (56) A. Yes.

Q. And were there any other employees of the Keystone Finance Company?

A. Not so far as I know.

Q. There were none? A. No.

Mr. Teiser. I call attention, if your Honor please, to keep the record straight, to Trustee's Exhibit seven, already introduced, showing the ownership of the Keystone Finance Company in the Western Bond and Mortgage Company of the entire stock holdings.

Q. Miss Gallagher, was there any change in the stock ownership of the Western Bond and Mortgage Company from the time this tax return was filed until the Western Bond and Mortgage Company had a petition in bankruptcy filed against it? The date of the tax return is the 4th of March, 1931, and it was for the year 1930. Was there any change in the officers of the Keystone Finance Company after March, 1931?

A. After March, 1931, up until what time?

Q. Up to any time—up to the time of the filing of the petition in bankruptcy?

A. The only difference was Miss Smith resigned as a director.

(Testimony of Miss E. E. Gallagher.)

Mr. Teiser. I introduce the original deeds of the Russell Land & Livestock Co. to the Keystone Finance Company of the (57) property, mortgage on which was subsequently assigned to the Bank of California.

The deeds attached together were marked Trustee's Exhibit 15. Nov. 9, 1936.

Mr. Greene. The property of the Keystone consisted of two parcels of land and the mortgage covered the two parcels, but it was all in one grant.

Mr. Teiser. At the time these deeds were given they made the conveyance in two parcels on December 20, 1929, both of them. It consisted of two parcels, as you will see, and when mortgaged to the Massachusetts Mortgage Company it was likewise in two parcels. They did not unite them in one instrument until I think the Ochoco came into it. I introduce these two deeds and have asked they be marked as one exhibit, fifteen. I would now like to introduce certified copies of the mortgages upon these two pieces of property from the Keystone Finance Company to the Western Bond and Mortgage Company, both of which mortgages are dated December 20, 1929, the



same day the deed was given to the Keystone, and these show they were recorded on the 28th day of December, 1929 that is, the deed on the Russell land, Trustee's Exhibit 15, and the mortgages which I am about to offer, both were recorded on December 28, 1929, at three o'clock p.m. In other words the deeds and mortgages were given and recorded at the same time. I ask that the mortgages be marked. (58)

\* \* \* \* \*

(Page 306)

Q. Miss Gallagher, I ask you to look at this minute book identified as Keystone Finance Company's minute book, and ask you whether or not the first or top sheet is not the record of a special meeting of the board of directors of the Keystone Finance Company and the time given for the meeting is not Portland, Oregon, February 11, 1932, at the hour of two p.m.? A. Yes.

Q. Were these minutes signed by you as president and Miss Thibodeaux as secretary?

A. Yes.

Q. Of the Keystone Finance Company?

A. Yes.

\* \* \* \* \*

**TESTIMONY OF R. ERICKSON**

(Page 330)

Q. Have you made an examination of the books of the Western Bond and Mortgage Company and

affiliated companies which we have mentioned here?

A. Certain of the accounts, yes.

Q. Have you examined them in regard to the principal transactions so far as they relate to the Russell Ranch and the transactions between it and the Western Bond and Mortgage Company and the Massachusetts Mortgage Company involved in the transfer to the Bank of California?

A. Yes I have.

(Testimony of R. Erickson.)

Q. Will you state from your examination of the books and records of the Western Bond and Mortgage Company what the voting stock of that company was in January, February and March, 1932?

A. Six thousand shares of common stock.

Q. Was there some preferred stock?

A. Four thousand shares of preferred stock outstanding.

Q. Did that preferred stock have voting power?

A. It did not. The stock contained a provision it did not participate in the voting unless three semi-annual dividends had been passed.

Q. Had three semi-annual dividends been passed at that time? A. They had not.

Mr. Thompson. Is that from the books?

Q. What dividends had been passed?

A. The last dividend paid was for December 31, 1930, and the next (86) dividend would be payable June 30th, 1931.

Q. And the records show the dividends were paid

on December 31, 1930? A. Yes.

Q. There has been introduced in evidence as testimony and marked Trustee's Exhibit 17 satisfaction of two mortgages running from the Western Bond and Mortgage Company to the Keystone Finance Company, the satisfactions being each dated the 13th of February, 1932, one satisfaction for the mortgage of \$77,500 and the other of a mortgage of \$72,500, both satisfactions recorded March 2, 1932, at 4:50 p.m. I will ask you whether or not the books show that the Western Bond and Mortgage Company received any consideration from the Keystone Finance Company for the satisfaction of these mortgages?

A. The Western Bond and Mortgage Company received nothing from the Keystone Finance Company to satisfy either of these mortgages.

Mr. Thompson. Move to strike the answer as not responsive.

Mr. Teiser. My question will show I asked what the books show.

A. The books do not show any consideration was received.

Q. The books as to this transaction were pretty thoroughly examined by you? A. Yes.

Q. And do the books show each transaction pretty fairly plain from time to time? A. Yes. (87)

Q. Every indication of being well kept?

A. Yes I would say the books were well kept.

Q. Do they show that any consideration was ever paid by the Keystone Finance Company for the satis-

faction of these mortgages?

A. I found no record of it.

Q. Would you or would you not say from the books and records that no consideration was paid for these satisfactions by the Keystone—books of the Western Bond and Mortgage Company; let me put it this way: Then would you say from an examination of the books and records of the Western Bond and Mortgage Company no consideration was paid by the Keystone Finance Company to the Western Bond and Mortgage Company for the satisfaction of these mortgages?

A. I found no record of any such consideration from the Keystone.

Q. You found no record of any consideration being paid?

A. No. records of any consideration being paid.

\* \* \* \* \*

(Page 353)

By Mr. Thompson:

Q. You have answered a number of interrogatories by counsel for the Trustee, after stating you examined the books of the Western Bond and Mortgage Company, to the effect that something included in your statement was not in the books; when you made such statements did you include the books of the subsidiary companies?

A. Yes I included the books of all the companies as far as I examined them.

Q. Have your examination of all of them been thorough enough to say that your statements do not

appear in any of the books of the subsidiary companies?

A. Concerning the transaction here, yes.

Q. You were going to bring me some sheets showing financial transactions between the Keystone and the Western Bond. I may not want to use them, but I wanted to take a look at them.

(Witness produces certain papers)

Q. Mr. Erickson, I have a little difficulty or maybe I am not competent to understand these four sheets you have handed me. What are they taken from?

A. These are from the bills receivable of the Western Bond and Mortgage Company. Either receivables or payables, they included them at the time under one control some time and under another at other times.

Q. Just for my information these are folio references?

The Court. You had better introduce them in evidence so you can identify what you are talking about in the record. (108)

Q. I hand you a sheet marked Respondent's Exhibit B for identification, and ask you if that is a sheet from the ledge of the Western Bond and Mortgage Company covering the accounts of the Keystone Finance Company with respect to the two Mortgages and notes that are involved?

Mr. Teiser. What two mortgages?

Mr. Thompson. Involved in this. You understand what I mean, don't you Mr. Erickson, and I think the court understands.

Mr. Teiser. I agree with you for the time being.

A. This is a ledger sheet of the Western Bond and Mortgage Company in which they recorded the transaction wherein they took the mortgage or mortgages from the Keystone Finance Company for one hundred and fifty thousand dollars covering the Russell Ranch, and this was accomplished in January, 1930.

Q. Did you find similar entries in the books of the Keystone Finance Company?

A. There are no books of the Keystone Finance Company.

Q. You have not been able to find any books of that Company at all? A. I have not.

Q. The third column represents the charges and the fourth the credits. Does that mean the Keystone was given credit on the Western Bond and Mortgage Company books for the \$150,000?

A. It does. (109)

Q. And the charges are withdrawals from that account?

A. They are disbursements made by the Western Bond and Mortgage Company on that account.

Q. Do the books show what the disbursements were made up of?

A. The books shows they are checks issued to the Keystone Finance Company.

Q. Did you find any books at all showing what they may have been used for by the Keystone?

A. I found none at all.

Q. The expenses are apparently to the subsidiary



by the Western Bond and Mortgage Company?

A. Yes, disbursements made on that account by the Western Bond and Mortgage Company.

Q. And whether that money was used by the Western to retire its obligations or for some other purpose you do not know; the books do not show?

A. I could not tell you except what is there.

Q. No record at all *the* show what they were used for? A. None at all.

Q. Did you find anything in the Keystone account to indicate that the money was expended for the Keystone as distinguished from the Western Bond and Mortgage?

A. There is nothing to show what became of it.

Q. You have no Keystone books at all?

A. No.

Q. You found nothing to explain the transaction as far as the (110) Keystone is concerned or show its receipt of it. A. I have nothing.

Q. You have some records showing there was a corporation? A. In the minute book.

Q. You found nothing in the minute book to show the expenditure of the one hundred and fifty thousand on that day or after that date, or that would show the value of the Keystone Finance Company?

A. No.

Q. And you found nothing that would show value in the Keystone Finance Company on that date or thereafter or to account for this money. A. No.

Q. So, so far as your investigation has gone you

do not know whether that money was expended for purposes of the Western Bond and Mortgage Company or for purposes of the Keystone Finance Company?

A. I don't know what was done with it.

\* \* \* \* \*

# TESTIMONY OF T. G. GREENE

(Page 402)

By Mr. Teiser :

Q. You say you went up to the court to hear these lawsuits?

A. I did not hear any of the suits. I heard arguments.

Q. Did you examine the papers in the cases at all?

A. Some I did, I read the petition in intervention, and one of the later petitions filed by Mr. Mott on behalf of the Corporation Commissioner in August of 1934.

Q. That was long after?

A. It had nothing to do with it at all.

Q. But before this last move was made you heard the arguments, and I think you said one in the State court?

A. In Judge Hall Lusk's department, and also before Judge McNary.

The Court. When were these suits you refer to?

A. One was commenced in March, 1931, and the other one in April, 1931, the principal one I think. There were four or five others.

Q. Did you see the complaints in these cases?

A. No only just to see who the parties were.

Q. You heard the argument but didn't look up the complaints? A. Yes. (157)

Q. Why did you go up to hear the arguments?

A. I knew it was the company in which O'Flynn was interested.

Q. Why did you go? Why was that?

A. Because the Bank of California was trying to get some additional security from the Western Bond and Mortgage Company.

Q. Did you know of this suit against the Western Bond and Mortgage Company brought by Allen McCurtain? A. Yes that was one of them.

Q. And another brought by Carl Little?

A. Yes.

Q. And the John Brocker suit brought in the United States District Court? A. Yes.

Q. Colonel Clark was engaged in this suit, was he not?

A. There were eight or ten lawyers participating in the argument.

Q. Don't you know that the charge was made in that suit that the Keystone Finance Company was a mere dummy of the Western Bond and Mortgage Company.

A. I didn't know it was charged in the complaint. I heard it, I think from some lawyer up there.

Q. You say it was a mere blackmailing scheme on the part of some of the certificate holders?

A. I didn't say that. I said I heard some of the lawyers or it may have been Mr. O'Flynn say that.

Q. You wanted to find out what was being done?

(158)

A. I wanted to get the facts if I could.

Q. Did you think that Mr. McCurtain and Mr. Little and Colonel Clark were engaged in a blackmailing scheme?

Mr. Thompson. I object to that. it is improper.

The Court. Objection sustained.

\* \* \* \* \*

(Page 407)

Q. I notice in this letter of yours that you ask for certain resolutions of the board of directors?

A. Yes.

Q. In the third paragraph you ask for a resolution of the board of directors of the Keystone Finance Company? A. Yes.

Q. I understood you to say you saw these resolutions?

A. Yes I saw them. they showed them to me but I wanted certified copies of them.

Q. In your answer to Mr. Thompson you said you had not seen this exhibit 19. I ask you whether or not— A. I never saw this.

Q. It is not one you saw?

A. I did not see it.

Q. Will you look through the Keystone Book?

A. I did not see it in the book. It is not there.

Q. Do you say you ever saw this?

A. No. (161)

Q. You never saw it?      A. I never saw it.

Q. What makes you think you never saw it?

A. The figures in there, *eight*-five thousand dollars of the preferred stock, that is one thing that makes me know I never saw it. I never saw that, it was not furnished to me.

Q. Have you copies of the one you did see?

A. I don't know if I have or not.

Q. You had a copy of the Ochoco one, did you not?

A. That is in the abstract.

Q. I ask for it?      A. I will look it up.

Q. Have you your papers here?

A. Yes but it is not here, no use to look for it, I did not see that, It was just a short resolution, no recitals in it except to authorize the making of the satisfaction of mortgage.

Q. I am not speaking of the satisfaction of mortgage. I am asking about the transfer of the property, to the writing here, eighty-five thousand shares of the preferred stock of the Western Bond and Mortgage Company and other valuable consideration, and it appearing that the said offer was attractive and the board having considered the same, it was moved and seconded the following resolution be adopted: Resolved, that this company accept from the Ochoco Farms Corporation eight hundred and fifty shares of the preferred capital stock of the Western Bond and Mortgage Company and other valuable consideration

in full consideration (162) for the properties owned by it and located in Crook County and known as the Russell Ranch.

A. I never saw that resolution before.

Q. Of the preferred capital *capital* stock—that is the preferred stock of the Western Bond and Mortgage Company. The resolution reads on, for the properties owned by it and located in Crook County and known as the Russell Ranch, make a proper deed of conveyance to the Ochoco Farms Corporation.

A. I think I saw that one. That sounds familiar.

Q. You say you saw that one?

A. The one you just read.

Q. That is what I am reading, right there, Exhibit 19. A. You didn't read all of that.

Q. That is a resolution authorizing the transfer of the Russell Ranch?

A. Yes, apparently it is so, but I say that is not the one furnished to me.

Q. Are you positive of that? A. Yes.

Q. Will you look through your papers and see which one you have?

A. I am sure that I have it, but it is not here. It may be attached to my work sheet on the title examination, and I haven't that here. I brought the original abstract but not my work sheets.

Q. You saw all the resolutions, you say you saw all of them? When you went through the book or some place you say you saw them? (163)

A. Yes.



Q. You saw all the resolutions you asked for at some time?     A. I did.

Q. All right, let us see. Exhibits seventeen, eighteen, twenty and twenty-one are certified copies of different documents authorized by these corporations, and resolutions were passed for such authorization. Exhibit 18 is a copy of the deed of the property by the Keystone Finance Company to the Ochoco Farms Corporation; Exhibit 20 is the mortgage of the Ochoco Farms Corporation to the Massachusetts Mortgage Company, and Exhibit 21 is where the Massachusetts Mortgage Company gave the assignment of the mortgage to the Bank of California?

A. Yes, I have seen them.

Q. You had the abstract of title and had the original deeds in escrow?

A. I don't know about these deeds.

Q. Where is that paper?

A. Do you mean the one I gave to Mr. O'Flynn?

Q. It was here a moment ago.

A. I have my copy of it.

Q. You had the mortgages of the Keystone Finance Company to the Western Bond and Mortgage Company?     A. I did have.

Q. You have a memorandum of it here on this receipt.     A. Yes. (164)

Q. That is Trustee's Exhibit 16?     A. Yes.

Q. Then you have the conveyance of the Keystone Finance Company to the Ochoco Farms Corporation; is that right?     A. I had that deed.

Q. And that is Exhibit 18?

A. I don't know what the exhibit is, but I had it.

Q. Won't you check it up?     A. I had it.

Q. Then you had the mortgage executed by the Ochoco Farms Corporation to the Massachusetts Mortgage Company which is Trustee's Exhibit 20?

A. Yes.

Q. And then you had the assignment of mortgage to be executed by the Massachusetts Mortgage Company to the Bank of California?

A. It was not that assignment.

Q. What assignment did you have?

A. It was not delivered to me, it had not been executed, there might have been a copy of an assignment but it was not this assignment here.

Q. Who was that executed by?

A. I don't think it was at all at that time, if it was anybody it was Mr. O'Flynn and that one I sent back.

Q. All these papers mentioned in this particular receipt, (165) with the exception of the two original mortgages, were recorded by you or on your behalf, at the same time, and were returned to you, were they not?

A. I can't tell by these copies, no showing they were returned to me.

Q. I have a letter from the clerk saying they were returned to you?

A. If the clerk says so, it might be so.

\* \* \* \* \*

## TESTIMONY OF H. E. ALWARD

(Page 412)

Q. Have you the credit file of the Western Bond and Mortgage Company? I don't want the whole file; is there anything in it about this particular loan?

A. I don't think there is anything in it. The last entry is July 10, 1932, livestock paper of the Western Finance Company.

The report produced by the witness was introduced in evidence and marked Trustee's Exhibit 30.

Mr. Teiser. I want to ask you some questions about this I think, Mr. Alward.

Mr. Thompson. It is merely things about which Mr. Alward testified about. I call it to the attention of the court.

At 3:30 p. m. the Court declared a recess of five minutes, after which the hearing continued as follows:

Mr. Teiser. If you want to let this file go in for me use what I need to use in it, it will be all right.

A. I do not know anything about it.

Mr. Thompson. We will furnish a witness to identify that if you want it identified.

Witness excused.

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Mr. Teiser. I would like to have it identified.

Mr. Thompson. It is a part of our files, when it was (168) compiled I don't know.

Mr. Teiser. The dates are on here.

Mr. Thompson. That is our credit file.

Mr. Teiser. I would like to introduce this credit file.

Mr. Greene. The whole thing?

The Court. Introduce it with permission to withdraw it.

Mr. Teiser. I don't want to be arbitrary. It may be withdrawn if needed.

Mr. Greene. The Bank examiner some times wants those things.

Mr. Teiser. I want to see these newspaper clippings referring to these various suits.

Mr. Thompson. I object to introducing the newspaper clippings as testimony.

Mr. Teiser. I don't want to be arbitrary with Mr. Greenwood or with anybody, or counsel. The attorneys have the credit file and I think it can be withdrawn at any time if he wants it, and if it left with the court I can come up and see it and get what I want from it.

The Court. The Western Bond and Mortgage Company is out of business and probably won't have any need for it, as far as that is concerned. I think it may be introduced in evidence with permission to withdraw it at any time.

Mr. Teiser. I introduce the file of the Bank of California (169) of Western Bond and Mortgage Company as presented here upon request.

The file was received and marked Trustee's Exhibit 31, Nov. 10, 1936.

## GEORGE M. McBRIDE

the Trustee herein, being produced as a witness in behalf of The Bank of California, Respondent, and, having first been duly sworn, was examined and testified as follows:

## Direct Examination

(Page 605)

By Mr. Thompson:

Q. Mr McBride, on the 13th day of July, 1939 I served a notice upon you to produce the books of account of the Keystone Finance Company. Have you produced them?

A. We have not produced them. However, they are available. You will find that Mr. Munro has gone over them quite carefully, and any of those that you want we are perfectly willing, of course, to have you bring them up here.

Q. We are not willing to do that. We have asked to have you (186) produce the books. We want them here, these particular ones I have asked to have brought here.

Mr. Teiser: Keystone Finance Company books?

Mr. Thompson: Keystone Finance Company books.

A. So far as my recollection goes, we have never been able to find those books. I don't know just what books you refer to, but my best recollection now is that Mr. Erickson and I looked for those books but were unable to find them, whatever they may be.

Mr. Teiser: Who is Mr. Erickson?

Mr. Thompson: I asked you in the notice for the

books of account of the Keystone Finance Company showing disposition of the moneys deposited in The Bank of California, N. A., when the mortgages in litigation in this matter were executed. Now, we have demonstrated here from the testimony of a bank employee that they did draw checks and dispose of money from that bank. Their accounts should show what they did with the money, what it was for, and those are the books we would like to have.

A. We are perfectly willing to produce them if we can find them, but I have——

Q. Well, have you made an effort to find them since this notice was served?

A. Well, I had prior to that, and, as I say, I went down and gave Mr. Munro, on your behalf, who is with the George Black Company, certified public accountants, gave him such assistance (187) as I could to locate any of those accounts which he wished to see or to produce, but my best recollection is that we found no regular books of account of the Keystone Finance Company.

Q. Did you ever find any books of account of the Keystone Finance Company?

A. Well, as I remember now, we did not. At least there were books of the Keystone Finance Company that Mr. Erickson and I endeavored to find to throw what light we could on the situation here, and we were unable to find anything which appeared of any use to us at that time. That is my best recollection now. It has been about three years since we did that.



Q. Just putting aside the question of what your judgment or what Mr. Erickson's judgment might be as to what was useful, did you find any books of account of the Keystone Finance Company?

A. Well, I wouldn't want to say whether we found any at all at this time. It has been, as I say, over three years, and we have about four tons of records there and we have so many records that my recollection just at this time,—I wouldn't say whether we found any books of account at all of the Keystone Finance Company.

Q. I will have to press you, George, just a little. Did you make an effort to find books of account of the Keystone Finance Company at all in response to this request?

A. Well, we made efforts originally to find them. I haven't made any special attempt since this, for the reason that Mr. (188) Munro went down there with me and we looked for any books which might throw any light on this subject, and I assisted him and felt that anything that we could find or that Mr. Munro could find had been found.

Q. Well, I now, then, renew the request to have the books of the Keystone Finance Company brought up here. Another request was that you bring each separate withdrawal check of the Keystone Finance Company showing the withdrawal and disposition of moneys that it might have had in the bank account. Have you brought those?

A. Not unless Mr. Munro has them here. He

brought some papers which he found there, subject to return, and gave his receipt for them, but I haven't the receipt with me now.

Q. Mr. Munro has no such checks, I will tell you that now.

A. Well, then there are no such checks here, and, to my knowledge, not in our records down there.

Q. And you now say that you have no such checks, and haven't had since you have been Trustee?

A. To the best of my knowledge, we have not. We have probably three or four tons of records, and to say definitely that they might not possibly be there would be making a pretty broad statement, but so far as I know, and from having gone over those records, I think very thoroughly, I would say that we haven't those checks.

Q. And have not had since you have been Trustee?  
(189)

A. We haven't had since I have been Trustee, unless we have them now, which would be to the best of my knowledge that we have not, but I might be mistaken, where there's four tons of records, and checks not being very large, and a possibility of misplacement.

\* \* \* \* \*

(Page 622)

Mr. Thompson: I will tell you gentlemen what I propose to do, if you don't bring the books up that we have asked for, if they don't bring them up here, I am going to put an expert on the stand and have

him testify from his notes, as the statute requires. We have asked for the books.

Mr. Teiser: Let it be understood here now that we make available those books to you. They are at the office in the Morgan Building, 738 Morgan Building, where your expert has (203) examined them, and they are there at your disposal.

A. Also in room 307 Worcester Bldg.

Mr. Thompson: Well, your Honor, are you going to adjourn court to that place down there?

Mr. Referee: Let me ask this: Can your experts and Mr McBride go down there and pick out the books you want?

Mr. Thompson: They probably can. We have a list.

Mr. Teiser: All right, we will give you everything you want here.

Mr. Referee: All right, then the order will be that Mr. McBride, accompanied by the experts, will attempt to locate and produce the books and the records required under the demand.

Mr. Thompson: All right.

The Referee: This order is made without determining the question of relevancy of any testimony that might be produced with reference to the books.

Mr. Thompson: Well, I can't go further without them, I will tell you that right now.

Q. Mr. McBride, you spoke about there being tons of those old records. Have you been through all of those, so that you know what is there?

A. I have been through them, I believe, through everything except the individual files, correspondence files, on canceled bond holders. There is a vast amount of those, thousands and (204) thousands of them, and they would produce no result by going through them, so far as I know, and unless there was some specific reason for it there seemed no reason for going through them. However, I have been through even thousands of letters and those various things, and I went through all those books to determine anything which appeared to be relevant. I can't keep it all in my mind now, of course, after three or four years' time. I spent a year, I suppose, going through all the various records in order to run down the various angles of the thing.

Q. Well, then the fact is that, aside from these large records of canceled bonds, was it, you said——

A. Well, their correspondence files.

Q. Dealing with that?

A. But for the most part are correspondence with bondholders relative to these bonds, and contain the canceled bonds which have been—where they have defaulted, and the bonds have been canceled.

Q. All right, and I beg your pardon for not having clear in my mind exactly what it was. Now, aside from those correspondence files, then, I will say that you have been through these records that you mention sufficiently so that you can tell whether a certain set of stuff—I don't care about the particular books—of Keystone Finance Company books are or are not

there?

A. Right now, from my recollection of having gone through them, I would say that very little of the Keystone Finance Company's (205) accounts which would reveal anything really of importance. Whether there is nothing there I wouldn't say.

Q. And then you also would be in position to say that you have been through the books sufficiently that you would know what it showed as to the disposition of the properties of the company, aside from this bond correspondence, from an examination of the books, what the Western Bond & Mortgage Company had done with all of its assets? I don't mean each little fine item, but I mean generally the larger stuff.

A. Well, most of the larger stuff perhaps I would. There were many things, I know, that never were explained or never very clear. Whether it was an absence of records or whether they didn't make proper records or what it was I am not sure.

Q. But you would know what the records do show, and have known that?

A. Well, I would know that. I have been through it at one time.

**DEFENDANTS' EXHIBIT 155**  
**PETITION IN INTERVENTION BY**  
**STATE OF OREGON**

IN THE DISTRICT COURT OF THE UNITED STATES  
 FOR THE DISTRICT OF OREGON

In the Matter of Western	)	
	)	In Bankruptcy
Bond and Mortgage Company,	)	No. B-16722
	)	PETITION IN
a corporation.	)	INTERVENTION

TO THE HONORABLE JOHN McNARY AND  
 JAMES ALGER FEE, Judges of the above  
 entitled court:

Comes now the State of Oregon and Charles H. Carey, Corporation Commissioner of the State of Oregon, and Gottlieb Jossi, Bessie Robinson, Louise B. McClintock, (formerly Louise Buford), and Wm. E. Koenig, who join herein, and by leave of Court first had and obtained, file this petition in intervention in the above entitled proceeding, and respectfully show your Honors and allege:

**I.**

That Charles H. Carey is the duly appointed, qualified and acting Corporation Commissioner of the State of Oregon.

**II.**

That the Western Bond and Mortgage Company, the alleged bankrupt, is a corporation duly organized and existing under and by virtue of the laws of the



State of Oregon, having its principal place of business in Portland, Multnomah County, State of Oregon, and that said corporation has been continuously domiciled in the State of Oregon since April 20, 1911; that a copy of its original articles of incorporation are hereto attached, marked Exhibit A, hereby referred to and made a part hereof; that its original authorized capital stock was \$100,000, divided into 1000 shares of the par value of \$100 per share.

\* \* \* \* \*

## XVI.

That said alleged bankrupt corporation conveyed, transferred, concealed and removed, or permitted to be concealed or removed, certain of its property with intent to hinder, delay and defraud its bondholders, creditors and investors, and said alleged bankrupt corporation has sequestered and removed from the State of Oregon and the jurisdiction of its courts many of the minute books, stock books and records of divers and sundry books of accounts of certain corporations in which the alleged bankrupt corporation holds controlling interest in the capital stock, to-wit: Beacon Investment Company, Central Realty Company, Insurance Building Corporation, Ljungdahl Products Company, Western Insurance Agency; and the books, records and accounts of certain other corporations dominated and controlled by the alleged bankrupt corporation, to-wit: Oakley Realty Company, Oak Service Company, Warm River Livestock Company, Bear Valley Livestock Company, Russell

Land and Livestock Company, Grand Ronde Livestock Company, Keystone Finance Company, Livestock Loan Company, and Ochoco Farms Corporation; that the officers of all of the aforesaid affiliated corporations are either the officers or employees of the alleged bankrupt corporation.

\* \* \* \* \*

### XVIII.

That when the Corporation Commissioner of the State of Oregon made his investigation, to the extent that he was able to investigate the affairs of the alleged bankrupt corporation, as hereinbefore alleged, which he was authorized to do under and by virtue of the terms of Section 25-1316, Oregon Code 1930, he reported the facts he was able to ascertain, as said statute provided, to the Attorney-General of the State of Oregon and to the District Attorney of Multnomah County for the purpose of having instituted such proceedings in law or in equity, in the name of the State of Oregon, to protect the interests of the stockholders, creditors and investors of the said alleged bankrupt corporation, as were deemed necessary.

That heretofore on November 25, 1931, there was filed in the United States District Court for the District of Oregon in bankruptcy, cause No. B-16722, an involuntary petition in bankruptcy against the said Western Bond and Mortgage Company, the alleged bankrupt corporation herein, which bankruptcy pro-

ceeding is now pending in said court. The United States District Court for the District of Oregon, by the filing of such petition in bankruptcy, thus has exclusive jurisdiction over the assets, affairs and properties of the alleged bankrupt corporation to the exclusion of all other courts. That said petition in bankruptcy was filed on November 25, 1931, by three alleged creditors, alleging to have provable claims, to-wit:

Warren Harvey, attorneys fees.....	\$500.00
D. R. Potter, wages due for work and and labor .....	\$ 90.00
Vincent & Vincent, service and printing .....	\$ 75.00

That thereafter on the 27th day of November, 1931, subpoena was issued and served upon the alleged bankrupt corporation. That on December 14, 1931, certain alleged creditors of said alleged bankrupt corporation duly intervened. Thereafter on December 15, 1931, the alleged bankrupt corporation filed its answer to the petition in bankruptcy, denying that it was insolvent. Thereafter on January 4, 1932, said alleged bankrupt corporation filed its demurrer to the petition of intervening creditors.

That thereafter on the 22nd day of June, 1932, the Judge of the United States District Court in said bankruptcy proceeding appointed MacCormac Snow as Special Master to take testimony and make findings of fact and recommendations to the Court in said bankruptcy proceedings, and ordered that the said

Special Master should require the respective parties to furnish him with such security, not to exceed the sum of \$1,000 for each side, as he may deem sufficient to secure the payment of a Master's fee, including the court reporter and other expenses incident to the reference. No such bond having been provided said MacCormac Snow resigned as Special Master, and thereupon on November 7, 1932, the United States Judge in said bankruptcy proceeding substituted Robert F. Maguire as Special Master in the place and stead of said MacCormac Snow, but no testimony has been taken by the said Master and none of the parties to said proceeding have deposited any bond or security for the payment of expenses of such hearing before such Master.

That on said 7th day of November, 1932, said United States District Judge made an order requiring the alleged bankrupt corporation to serve upon petitioners and intervening creditors a statement under oath, giving the names and addresses of all installment bondholders of the alleged bankrupt corporation, showing the number of bonds held by each bondholder and the number of such bonds, and a list giving the names and addresses of all general creditors of the alleged bankrupt corporation, showing the amount of indebtedness owing to each creditor, and requiring the alleged bankrupt corporation to furnish said statement within ten days from said November 7, 1932. Said alleged bankrupt corporation did not comply with said order.

aforesaid, and with knowledge of the pendency of said bankruptcy proceeding, consented to the substitution of said worthless securities so made by the officers of the alleged bankrupt corporation.

## XX.

That in many instances, without the order or permission of the United States District Court, the officers of the alleged bankrupt corporation have been settling with creditors of the said alleged bankrupt corporation, and preferring them in said settlements to the other creditors of the said corporation to the latter's loss and financial injury.

## XXI.

That at the date of the filing of the said petition in bankruptcy there was on deposit with the Lawyers Title and Trust Company, under the trust agreements aforesaid, which deposit was made by the alleged bankrupt corporation, two mortgages totaling \$150,000, covering real property known as the Russell Ranch, near Prineville, Oregon, of approximately 14,000 acres, which said mortgages covered all buildings, improvements and equipment on said land, and which said mortgages were of the probable value of \$150,000. That at said time the alleged bankrupt corporation was indebted to the Bank of California, National Association of Portland, Oregon, in a sum approximating \$118,000.

That the Keystone Finance Company, an Oregon corporation, was the record owner of the property



hereinbefore referred to as the Russell Ranch. That said Keystone Finance Company executed the mortgages upon said property to the alleged bankrupt corporation, which latter corporation in turn deposited the mortgages with the trustee as hereinbefore stated.

That on the 27th day of May, 1931, the said Keystone Finance Company, by supplementary articles of incorporation, changed its name to the Keystone Holding Company, with the principal office at 70 Broadway Street, Portland, Oregon, such office being also the office of the alleged bankrupt corporation. That the directors and officers of the Keystone Holding Company are also officers, directors or employees of the alleged bankrupt corporation, and said company while operating under the name of Keystone Finance Company or operating under the name of the Keystone Holding Company, has been at all times under the management and control of the officers of the alleged bankrupt corporation.

\* \* \* \* \*

## XXV.

That prior to and since the filing of the petition in bankruptcy herein, the alleged bankrupt corporation, through its officers, has wrongfully and unlawfully expended, wasted and dissipated its funds, securities and assets, and is hopelessly insolvent. That it is absolutely necessary for the preservation of the estate of the alleged bankrupt corporation that this Court appoint a receiver to take charge of the prop-



erty of the alleged bankrupt corporation, and that such receiver be instructed and directed by this Court to institute such proceedings in law or in equity as may be appropriate to set aside and annul the wrongful transactions of the officers of the alleged bankrupt corporation transferring the securities, property and assets of said corporation, and restoring the same to the estate of said alleged bankrupt corporation, and to institute such proceedings in law and equity as may be fit and appropriate to protect the interests of the stockholders, creditors and investors of the alleged bankrupt corporation, and to this end such receiver be authorized and directed to institute such appropriate proceedings, either in law or in equity, against the officers of the said alleged bankrupt corporation as may be deemed necessary.

\* \* \* \* \*

## XXVII.

Reference is hereby made to the affidavit of Charles A. Goodwin, Deputy Corporation Commissioner of the State of Oregon, hereto attached, who made an investigation of the books and records of the alleged bankrupt corporation, and reference is also hereby made to all of the records and files in the aforesaid bankruptcy proceeding.

WHEREFORE, your intervening petitioners respectively pray that your Honors will forthwith fix a date for hearing of this petition upon due notice to the alleged bankrupt corporation, and that upon

such hearing your Honors will forthwith appoint a receiver to take charge of all and singular the assets of said alleged bankrupt corporation within the jurisdiction of this Court, to hold and conserve the same during the bankruptcy proceedings and pending the appointment and qualification of a trustee, and that the said receiver be instructed and directed to institute such proceedings in law or in equity as may be appropriate to set aside and annul the wrongful transactions of the officers of the alleged bankrupt corporation transferring the securities, assets and property of said corporation, and restoring the same to the estate of said alleged bankrupt corporation, and to institute such proceedings in law and equity as may be fit and appropriate to protect the interests of the stockholders, creditors and investors of the alleged bankrupt corporation, and to institute such appropriate proceedings, either in law or in equity, against the officers of the said alleged bankrupt corporation as may be deemed necessary, and for such other and further relief or orders as may become necessary and proper in the premises.

I. H. VAN WINKLE,  
Attorney-General of Oregon,  
RALPH E. MOODY,  
Assistant Attorney-General,  
Attorneys for Intervening  
Petitioners.

UNITED STATES OF AMERICA, )  
 )  
 STATE OF OREGON, ) ss.  
 )  
 COUNTY OF MARION, )

I, Charles M. Carey, being first duly sworn, say that I am the duly appointed, qualified and acting Corporation Commissioner of the State of Oregon; that I am one of the intervening petitioners named in the foregoing petition; that I have read the same, and that the same is true, as I verily believe.

CHARLES H. CAREY,

Subscribed and sworn to before me this 2nd day of August, 1934.

EDWARD E. SOX,

Notary Public for Oregon.

My commission expires: Sept. 29, 1933.

(NOTARIAL SEAL)

IN THE DISTRICT COURT OF THE UNITED STATES  
 FOR THE DISTRICT OF OREGON

	)	No. B-16722
	)	AFFIDAVIT OF CHAS.
	)	A. GOODWIN IN SUP-
IN THE MATTER OF THE WEST-	)	PORT OF THE INTER-
	)	VENING PETITION OF
ERN BOND AND MORTGAGE COM-	)	THE CORPORATION
	)	COMMISSIONER OF
PANY	)	THE STATE OF ORE-
	)	GON FOR THE AP-
	)	POINTMENT OF A RE-
	)	CEIVER.

UNITED STATES OF AMERICA    )  
 STATE OF OREGON                ) ss.  
 COUNTY OF MARION             )

I, Chas. A. Goodwin, being first duly sworn upon oath say that I am the duly appointed, qualified and acting deputy corporation commissioner of the State of Oregon, and that I am an expert accountant; that at the instance, request and direction of Charles H. Carey, the Corporation Commissioner of the State of Oregon, from the 28th day of March, 1934, to and including the 5th day of May, 1934, I made an investigation and examination, so far as the same were available, of the corporate records of Western Bond and Mortgage Company, the alleged bankrupt, and of its books and accounts, and that from such examination it appears that the said alleged bankrupt corporation is insolvent, as is alleged in the intervening petition of the State of Oregon and the Corporation Commissioner of the State of Oregon, and the creditors therein named, who joined in said petition, and reference is hereby made to the said intervening petition and to all of its allegations;

That at the date and time the Lawyers Title and Trust Company was substituted for trustee in lieu and instead of the Portland Trust and Savings Bank, formerly Portland Trust Company of Oregon, under the provisions of the trust agreements mentioned and referred to in the intervening petition of the State of Oregon and of the Corporation Commissioner of the State of Oregon, there was delivered to

Lawyers Title and Trust Company by Portland Trust and Savings Bank sixty-four mortgages of a face value of \$601,401.71, and municipal bonds of the face value of \$30,500.00, and certificates of deposit of \$4,300.00, making a total of the face value of all securities of \$636,201.71, all of which mortgages, municipal bonds and certificates of deposit had been deposited with the trustee under the provisions of its trust agreements to secure the payment of its installment, single-payment and coupon bonds; that since the Lawyers Title and Trust Company received such securities, there has been withdrawn therefrom, by the alleged bankrupt corporation, many of said mortgages and other securities, and other mortgages and securities have been substituted therefor, but in some instances there has been withdrawn mortgages and other securities from said trustee by the alleged bankrupt corporation and for which withdrawals there has been no substitution; that some of such instances are as follows:

There was deposited by the alleged bankrupt corporation with the trustee, during the time that Portland Trust and Savings Bank was the trustee, a mortgage on the St. Clair Apartment House of Portland, Multnomah County, Oregon, and at the time the said mortgage was delivered to the Lawyers Title and Trust Company, which succeeded the Portland Trust and Savings Bank as trustee, there was a balance due upon said mortgage of \$44,857.50, and on February 28, 1931, the alleged bankrupt corporation withdrew



from said trustee, Lawyers Title and Trust Company, said mortgage, at which time there was due thereon the sum of \$44,512.50, and the said alleged bankrupt corporation did not then, nor has it at any time since, substituted any mortgage or other security of any kind whatsoever in lieu of or in place of the said mortgage so withdrawn by it on said 28th day of February, 1931. The said mortgage so withdrawn by said alleged bankrupt corporation was sold on April 19, 1931, to the Portland Trust and Savings Bank (the former trustee) by said alleged bankrupt corporation at a discount of \$10,187.50, in an apparently collusive transaction; that the said mortgage was equal in value, at the date of its said sale to the Portland Trust and Savings Bank, to \$44,512.50, the full amount of the balance due thereon;

That the two mortgages, in the respective amounts of \$77,500.00 and \$72,500.00, totaling \$150,000.00, on the Russell Ranch, deposited with the trustee, mentioned and referred to in the petition of intervention by the State of Oregon and the Corporation Commissioner, were probably of the value of the amount due or to become due on said mortgages; that the officers of the alleged bankrupt corporation withdrew from the trustee said two mortgages or or about February 29, 1932, which was since the date of the filing of the petition in bankruptcy against the said alleged bankrupt corporation; that the officers of the alleged bankrupt corporation, after they had withdrawn the said mortgages, cancelled and released the said mortgages,



and substituted with said trustee for said two mortgages withdrawn (a) mortgage for \$135,000.00 on nine hundred acres of diking district land in Wahkiakium County, State of Washington, on which there was due a large amount of diking district assessments and delinquent taxes, which have since accumulated to \$36,656.97, and this land has now all been ordered sold to satisfy judgments for said taxes and assessments; (b) mortgage for \$90,000.00, covering eight hundred lots in the City of Bend, Oregon; that this mortgage is far in excess of the value of the property that it covers, and that not many years prior to the execution of the last mentioned mortgage, the property so mortgage was sold for \$10,000.00 in satisfaction of a mortgage thereon, of which the balance due was \$45,000.00; that the record title of this property was acquired by Realty Securities Corporation, a corporation owned and controlled by the officers of the alleged bankrupt corporation, and it was the said Realty Securities Corporation that executed the mortgage to the alleged bankrupt corporation for the said sum of \$90,000.00, which was then deposited with the Lawyers Title and Trust Company, as trustee, as one of the mortgages substituted for the aforesaid mortgages withdrawn from the trustee upon the aforesaid Russell Ranch property; that this last mentioned mortgage is of very small value, if it has any;

That it has been the practice of the officers of the alleged bankrupt corporation, before and since the filing of the petition of bankruptcy against the said

alleged bankrupt corporation, to withdraw from the trustee mortgages and other securities of value, and that whenever any mortgages or other securities were substituted for those withdrawn, such substitutions were of far less value than those withdrawn, and that this juggling by the officers of the alleged bankrupt corporation with the securities so deposited with the trustee was done in connection with and through the means of other corporations, which were either owned or controlled by the officers of the alleged bankrupt corporation;

\* \* \* \* \*

## EXHIBIT N

SPECIAL MEETING OF THE BOARD OF DIRECTORS OF THE WESTERN BOND & MORTGAGE COMPANY, HELD AT THE OFFICE OF THE COMPANY IN PORTLAND, OREGON, FEBRUARY 11, 1932, AT THE HOUR OF TWO P. M.

All of the Directors being present, notice of time and place of meeting was waived.

The President of the Company called the Board's attention to considerable negotiations with the Bank of California, to which bank this Company is indebted in approximately the sum of \$118,000.00 by reason of rediscounts made to such bank. He likewise presented to the Board various letters of considerable threatening nature and disclosed that for a period of time last past great pressure was being put on this Company

by the Bank in an endeavor to have this Company liquidate such obligation. He also disclosed the fact that the Company through its officers had done everything possible to satisfactorily adjust matters with the Bank and pay this obligation and that it would be necessary to borrow from the Massachusetts Mortgage Company certain money or securities to the extent of \$35,000.00, which had already been done and which had been pledged to the Bank of California by said Corporation, and likewise that it was necessary that additional funds be secured to pay the balance due and that it would be necessary to secure funds to pay taxes on the property known as the Russell Ranch which was mortgaged to this Company; to secure funds to pay the annual rental on the lease and secure additional funds to operate the property if possible, and that various negotiations have been carried on and under the present market the said Russell Ranch was being run at a considerable loss and that same was unable to meet its interest and that the mortgage was being criticized as being in excess of the actual value of the said Russell Ranch; that a Corporation, known as the Ochoco Farms Corporation, had acquired the ranch and that it was necessary to borrow funds to the extent of approximately \$28,000.00 from said Ochoco Farms Corporation, which funds so borrowed together with the amount advanced by Massachusetts Mortgage Company, and together with what sums could be secured from the liquidation of certain sheep mortgaged to this Company and rediscounted

to the Bank of California, would pay the entire indebtedness and would leave this Company with a liability in excess of \$118,000.00; and the President therefore asked that the Company ratify the loan heretofore made from the Massachusetts Mortgage Company in the extent of \$35,000.00 and that this Company borrow from the Ochoco Farms Corporation approximately \$28,000.00 on such terms as could be obtained to the end of satisfying the claim of the Bank of California against this corporation. All of which seemed to the President to enure to the benefit of the stockholders and bondholders of this Corporation.

The Secretary, E. F. O'Flynn, presented to the Board the various facts concerning those two certain mortgages on the property owned by the Keystone Finance Company and known as the Russell Ranch, the said mortgages being in the sums respectively of \$77,500.00 and \$72,500.00, aggregating \$150,000.00, and that considerable criticism of the Company and liquidation had been instituted by reason of the supposed excessive values of said property, and further, that the Keystone Finance Company had conveyed the property to the Ochoco Farms Corporation, which latter corporation was now the owner, and which corporation was desirous of having said mortgages satisfied. He further informed the Board that the Ochoco Farms Corporation are the owners of a certain mortgage on property located in the town of Bend, Oregon, which property was owned by the Realty Securities

Corporation, an Oregon Corporation, and that said property was appraised at approximately \$200,000.00 on the present market, such appraisal being made by five of the leading realtors in the town of Bend, Oregon, and that said mortgage was in the sum of \$90,000.00. He also represented to the Board that the Ochoco Farms Corporation was the owner of a certain mortgage on property located in Wahkiakum County, Washington, which property had been appraised by responsible realtors and bankers as being worth approximately \$270,000.00, and that said property was owned by the Realty Securities Corporation and the mortgage held by the Ochoco Farms Corporation was in the sum of \$135,000.00; that the Ochoco Farms Corporation were ready and willing to convey to this Company both of said mortgages in full payment and satisfaction of the two mortgages on the Russell Ranch, which certain mortgages are in the following amounts: One in the sum of \$77,500.00 dated December 20, 1925; and in the sum of \$72,500.00, dated December 20, 1929; and also in full payment of and satisfaction of that certain mortgage in the sum of \$58,000.00 made by Lake Lucerne, Incorporated, and now held by this company, and in full satisfaction and payment of bonds aggregating the sum of \$17,500.00, known as the Kennydale Water Company bonds, of Kennydale, Washington.

After some discussion, the following resolution was made and seconded:



RESOLVED, that this company accept from the Ochoco Farms Corporation the mortgage on properties located in Bend, Oregon, securing a note in the sum of \$90,000.00, and which mortgage is a first lien on approximately 800 city lots in the town of Bend, Oregon, which have been appraised at approximately \$225.00 per lot; and a note and mortgage in the sum of \$135,000.00, which note and mortgage is secured by approximately 900 acres of land located in the County of Wahkiakum, Washington, and appraised at approximately \$270,000.00, in full payment and satisfaction of those two certain mortgages made and executed by the Keystone Finance Company, in the respective sums of \$77,500.00 and \$72,500.00 and which mortgages represent land located in Crook County, Oregon, and known as the Russell Ranch, and in full payment and satisfaction of that certain mortgage in the sum of \$60,000.00 made by Lake Lucerne, Incorporated, and secured by certain properties in said mortgage described, and in full payment of bonds of the face value of \$17,500.00, issued by the Kennydale Water District, of Kennydale, Washington, known as the Kennydale Water Company bonds; and be it further RESOLVED that the President and Secretary, or President and Assistant Secretary make a proper satisfaction of the mortgages in the sum of \$77,500.00 and \$72,500.00; and be it further RESOLVED that the President and Secretary, or President and Assistant Secretary make a proper satisfaction of the mortgage executed by Lake Lucerne, Incorporated, in the sum of \$58,000.00, or a satisfaction of the same as directed by representatives of the Ochoco Farms Corporation, and a delivery of bonds aggregating the sum of \$17,500.00;

AND BE IT FURTHER RESOLVED that the proper officers of this Company be directed to borrow from the Ochoco Farms Corporation the sum approximately \$27,000.00 on such terms as



they can best obtain, and be it further RESOLVED that the action of the officers heretofore borrowing from Massachusetts Mortgage Company the sum of \$35,000.00, which sum is in the form of a second mortgage on Seattle property and which has been accepted at par by the Bank of California as an obligation of this Company, be ratified and approved, and that the proper officers of this Company make and execute any note or obligation or pledge to secure the said Massachusetts Mortgage Company.

The foregoing resolutions were unanimously passed and the proper officers directed to execute the proper instruments relative to the mortgages and to deliver the bonds.

There being no further business, the meeting adjourned.

Signed W. E. Johnson

President

Attest E. F. O'Flynn

Secretary

.....AND BE IT FURTHER RESOLVED, that the President and Secretary, or President and Assistant Secretary, make the proper satisfaction of the said mortgages made and executed by the Keystone Finance Company in the respective sums of \$77,500.00 and \$72,500.00 and cause the same to be recorded;

The foregoing resolution was unanimously passed and the proper officers directed to execute the proper instruments relative to the said mortgages, et cetera.

There being no further business, the meeting adjourned.

Signed W. E. Johnson  
President

ATTEST:

E. F. O'Flynn  
Secretary.



In the United States  
**Circuit Court of Appeals**  
For the Ninth Circuit

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,

*Appellant,*

vs.

C. H. FARRINGTON,

*Appellee.*

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**APPELLANT'S REPLY BRIEF**

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Upon Appeal from the District Court of the United  
States for the District of Oregon.

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**FILED**

**MAY 22 1946**

SIDNEY TEISER,  
WM. G. KELLER,  
(Teiser & Keller)  
*Attorneys for Appellant.*

**PAUL P. O'BRIEN,**

**CLERK**



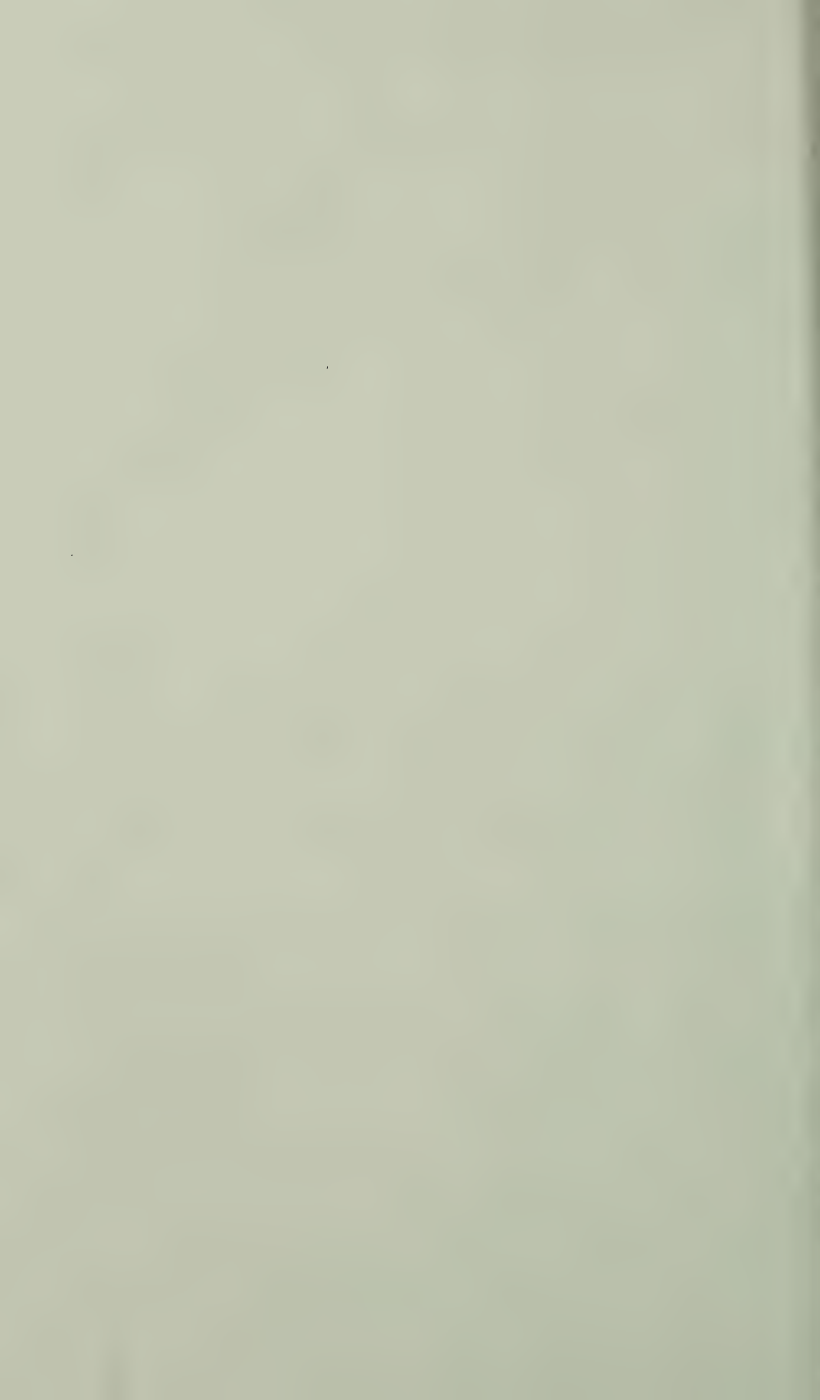


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*Appellee.*

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**APPELLANT'S REPLY BRIEF**

---

Upon Appeal from the District Court of the United  
States for the District of Oregon.

**ANENT, APPELLEE'S PRELIMINARY  
STATEMENT**

The appellee, C. H. Farrington, in his Brief, pp. 5 & 6, is critical of the Appellant's Brief in that it is asserted that appellant presents therein his case on the theory that Farrington had been a party to the fraud charged in the complaint. We do so present our case, for obviously under the pre-trial order segregating the trial of the issues of fraud and of limitations and ordering the trial of the latter issue first, the assumption must be made that the frauds alleged in the complaints are true. On no other theory could

the issue of limitations (in which we include laches) be determined. Obviously the court under the order of segregation (Tr. 58) was compelled to assume that the frauds asserted were provable in order to determine whether the statute of limitations had run against suit for recovery.

In the course of the argument in Appellee's Brief, Appellee's attorney, says (p. 6),

"Although charges of fraud have been hurled against this defendant since 1931, there has never been any adjudication of misconduct on defendants' part in any proceeding, and none in the case at bar."

Such a statement is unwarranted. There is nothing in the Record here, (and that is what we are trying this upon) to justify the statement (1) "that there never has been any adjudication of misconduct on defendant's part in any proceedings" or to justify the statement (2) "that charges of fraud has been hurled against the defendant since 1931."

Moreover, we are at a loss to appreciate the statement that "fraud is never presumed" appearing on the same page of appellee's Brief. May we venture the suggestion that where an officer owning a substantial majority of the stock of a corporation obtains a transfer of property of the corporation to himself that a presumption of fraud follows.

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In his Brief, after the preliminary statement, C. H. Farrington urges:

- (1) That the appellant's Assignments of Error are insufficient to present any question for the consideration of this Court,
- (2) That the findings of fact are not amenable to attack, since some substantial evidence was adduced to support them.
- (3) That the evidence adduced showed also that the trustee was guilty of laches barring the suit, and
- (4) That the evidence adduced shows that the Trustee in Bankruptcy, appellant, had failed to pursue with reasonable diligence information which had come to him, which information if pursued would have brought knowledge of the frauds alleged, thus barring the suit.

Let us consider these contentions of the appellee in the order stated.

## **SUFFICIENCY OF ASSIGNMENTS OF ERRORS**

What, we ask, is the purpose of the requirement that errors be assigned? Naturally, so that the Appellate Court may know just what particular error is claimed to have been made by the trial court which justifies the appellant in the belief that the cause should be remanded or the judgment be reversed, and also so that the appellee may be able to know and to meet the specific attacks of the appellant. Thus, it is held insufficient to assign as error merely that the Court entered a wrong decree (*Cohen v. U. S.* and

*Squibb v. Mallueckrodt Chemical Works*, cited and quoted from by Appellee in his Brief, p. 9), or that generally the trial court made wrong findings (*American Surety Co. v. Fischer W. Co.*, also cited and quoted from in Appellee's Brief, p. 8).

However, there is no such generality in the Assignments of appellant here questioned.

Certainly our Assignment I cannot be objectionable. It reads: "The Court erred in determining that the Oregon Statute was the applicable Statute" (see our Opening Brief, p. 18). Is that not specific enough? The determination involved solely a question of law. Is it possible that Appellee insist that we must point out the mental process of the Court that caused it to reach such a conclusion, which we assert to be wrong? We will stand on the assignment.

The next assignment proceeds on the assumption that the Court has determined the applicable statute to be the Oregon Statute prescribing limitation of two years from the discovery of the fraud. We assign in this Assignment (IIa) that the court erred in holding "that the Trustee had not brought the action within two years from discovery." (Our Brief p. 18). Then follows, shortly after in our Brief (p. 24) this statement "There is direct testimony to the effect that the discovery of the fraud occurred only within a month or two after bringing this action, and there is no testimony whatsoever of an earlier discovery."

The third assignment set forth in our Brief (p. 18)

3 Specification II(b), and that assignment states



that the Court erred in holding "that the information which came to the Trustee charged him with the duty to pursue it." It seems to us that there can be only one implication as to this assignment and that is that the inference which the court drew, was in law an erroneous inference, namely, that the information coming to the trustee charged him with the duty of pursuit. We maintain that such an Assignment of Error meets all the requirements of a sufficient assignment.

The fourth assignment (Our Brief, p. 19), being number II(c), assumes the finding by the Court that there was duty of pursuit, yet assigns as error the holding that "such information if pursued would have resulted in discovery at a time more than two years prior to the institution of the action here". We insist that such assignment is not amenable to the objection of generalization. Quite the contrary, it definitely points to error of law in the Court's holding that in the light of the evidence there would have resulted earlier discovery had the available information been pursued.

The last assignment, being numbered by us III, (Our Brief p. 19) assigns as error the Court's holding "That the Trustee was guilty of laches." That too, we maintain, is a sufficient specification of an error of law, since it is apparent that our position is that there were no facts on which such a finding could have been correctly made. (See discussion of Laches, Our Opening Brief, pp. 35-36.)

## AMENABILITY OF FINDINGS TO ATTACK

We are fully aware of the doctrine that where there is a conflict of evidence, and the court makes findings based on some evidence, even though the evidence on which the finding is made be meager and not preponderant, such findings will not be disturbed on appeal. But the findings of fact must be findings of *fact*, and not a mere inference from admitted or found facts or from uncontroverted evidence.

Moreover, it is immaterial that the inference or conclusion be called a finding. Such appellation is of no consequence.<sup>(1)</sup> Under such circumstance the Appellate Court is as well qualified to make the inference as is the trial court.<sup>(2)</sup> The subject thereupon becomes a matter of law, and not of fact.

Let us particularize: In the case at bar the Court under the title of Finding of Facts, states "Plaintiff had actual knowledge or was in possession of information which was sufficient to guide him to actual knowledge," (Finding III.) which information he "failed to pursue with reasonable diligence", "and which pointed to the transactions referred to in the Complaint". (Finding IV)

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(1) 5 C.J.S. Appeal and Error 1454, pp. 25-26.

(2) *Western Union Tel. Co. v. Brombert* (C.C.A. 9th) 143 F. (2d) 288, 290; *Stubbs v. Fulton Natl. Bank* (C.C.A. 5th) 146 F. (2d) 558, 560; *Murray v. Noblesville Milling Co.* (C.C.A. 7th) 131 F. (2d) 470, 474; *Kuhn v. Princess Lida*, (C.C.A. 3rd) 119 F. (2d) 704, 706; *Shultz v. Mfg. & Traders Trust Co.* (C.C.A. 2nd) 128 F. (2d) 889, 901.

Now is not this whole statement an inference rather than a finding? In the first place, if the plaintiff had "actual knowledge" of the transactions referred to in the complaint, and if he had possession of information which was sufficient to guide him to knowledge" which if followed through with reasonable diligence would have spelled discovery, then the trial court should not have made his "findings" in these regards in the conjunctive. A Court does not correctly make a "finding either or". But that is just what the trial court here did, for he says: "plaintiff had actual knowledge *or* was in possession of information". Obviously, the Court was merely being argumentative, and of course no finding should, or properly can, have such character.

We assert, with assurance, that there was not a scintilla of evidence that the trustee had actual knowledge at any time prior to a few months before suit was brought. In fact all the evidence on that question is to the contrary (Tr. pp. 95-96). Consequently, the so-called "finding" to this effect was either erroneous, or it was merely setting the stage for an inference to the effect that if the trustee did not have actual knowledge he should have had it. That is, we contend, the exact significance of the Court's Findings III and IV. They are really not findings at all, but merely an inference or conclusion from the admitted facts based on undisputed testimony. Such inference, or a contrary one, the Court here can as well draw as could the trial court.

The last "finding" of the court, to which we assigned error, is the finding (VI) that "Prior to bringing of this action, participants in the transactions . . . and others who had known the material facts had died, and defendant was deprived of a means of defense through their evidence."

We maintain that such a finding is too general a one to make it anything more than a conclusion. What facts were known to whom? Who had died knowing **such** fact? Would such facts have been favorable to defendant? Was the defendant deprived of the means of defense by the fault of the plaintiff or merely by the act of God—death?

But, be that as it may, our more specific objection to this "finding" is that it is not based on any evidence. No testimony was introduced to the effect that those who were in any way connected with, or who participated in, the transactions would have given favorable testimony for the defendant. Mr. Arthur Spencer (whose only asserted connection was that he was attorney for the defendant) it was testified to, handled the legal phase of the Western Guaranty Stock transaction for Farrington (Tr. p. 254), but there was no testimony that he knew the facts concerning the alleged fraud asserted in plaintiff's complaint, or that he would have, if alive, testified favorably to defendant's defense. Mr. O'Flynn, it was testified, was also dead. He it was who represented the Massachusetts Mortgage Company, the intermediate purchaser in the alleged fraudulent Western Guaranty Stock deal (Tr. p. 257). But there was no testi-

mony that the facts which he knew would have been helpful to the defendant. (As a matter of fact, the death of Mr. O'Flynn was thought by us, for a time, to be disastrous to plaintiff in the proof of his case.) Judge Carey, it is asserted, is also dead. He was the Corporation Commissioner of the State of Oregon at the time of the transactions. But there is not the slightest intimation in the testimony (albeit, there is such intimation in Appellee's Brief, p. 21) that Judge Carey knew the slightest thing about the transactions set forth in the complaint, or that he could have testified favorably to defendant.

Referee A. M. Cannon is also dead. But it is not even claimed by either of the parties, much less is there any testimony, that Referee Cannon had the slightest knowledge of the transactions referred to. (In Appellee's Brief pp. 22, it is asserted that the death of A. M. Cannon made it impossible to challenge the truth of the testimony of the Trustee—though nothing is said about challenging the truth of like testimony of the trustee's attorney—to the effect that he directed that no objection be filed or pressed to the Government's claim for taxes until there were some assets available in the estate to pay at least a portion of the claim if allowed). The referee's death could only have prevented his testimony concerning the delay or promptness in the discovery of fraud—not in the establishing a defense concerning the fraudulent transactions of Farrington, which of course, was what the "findings" referred to.



Where, then, was the basis for the "finding" that "defendant was deprived of a means of defense" by the death of "the participants in the transactions referred to in the complaint, and others who had known the material facts"?

We maintain therefore, in this case, where the facts are not disputed as to what information came to the trustee, that the ultimate facts as to whether or not such information in the exercise of reasonable diligence should have been pursued and if pursued would have resulted in timely discovery, is a question which this court may determine as well as the trial court. As was said in the case of *Murray v. Noblesville Milling Co.* (C.C.A. 7th) 131 F. (2d) 470, 474 (ante)

"To be sure where the findings of fact is supporting by evidence and is not clearly erroneous it must be accepted by us but the rule does not operate to intrench with like finality the inferences or conclusions drawn by the trial court from its fact findings and we are free to draw the ultimate inferences and conclusions which the findings reasonably induce, and where the evidentiary facts are not in conflict or dispute, the conclusions to be drawn therefrom are for the appellate court upon review."

To like effect also is *Kuhn v. Princess Lida* (C.C.A. 3rd) 119 F. (2d) 704, 706 (ante), where it is said:

"Where the evidentiary facts are not in conflict or dispute, the conclusions to be drawn therefrom are for the appellate court upon review of the trial court's action . . . An incorrect conclusion by a trial court qualifies as a 'clearly erroneous'



finding, for the correction whereof on appeal Rule 52(a) specifically provides.”

## LACHES—NO EVIDENCE JUSTIFYING THE HOLDING

Appellant in its Brief takes issue with our statement that if the present action is not barred by the Statute of Limitation it is not barred by laches. We still insist that such is true in this particular case, and we again revert to the case of *Sedlak v. Sedlak*, 14 Or. 540, 541, quoted from in our Opening Brief (from which Appellee also quotes). There it is said,

“The general rule, without doubt, is, that no lapse of time or delay in bringing suit will be a bar to the remedy in equity, provided the injured party, during the interval, was ignorant of fraud, but the ignorance of such party must not have been negligent, for if by reasonable diligence fraud could have been discovered or ought to have been known, he will be deemed guilty of laches.”

Therefore, under the doctrine of that case, which is the doctrine of the authorities generally, if the trustee was ignorant of the fraud and such ignorance was not due to lack of diligence in making inquiry and then reaching discovery, he is not barred by laches. If, on the other hand, he were guilty, then he is barred by the Statute of Limitations, (assuming that the Oregon statute is the applicable statute). Thus we repeat the question of laches in the case is academic, for it cannot be invoked, if we were without knowledge or were diligent; and if we had knowledge or

were negligent, there is no need to invoke it, for the statute of limitation then bars.

Moreover, in this case there is not a scintilla of evidence that the delay was working a hardship on defendant. True, according to the evidence, several men, as heretofore pointed out, have died—Arthur Spencer, Edward F. O'Flynn, Judge C. C. Carey, and Referee A. M. Cannon. But in no instance was there any testimony that any of these men had any knowledge concerning the transactions complained of, or that if they did, their testimony would have been helpful to Farrington.

Farrington, again and again in his Brief, stresses the inability which might be caused by lapse of time, to assemble evidence showing the value of the property which in our complaint it is alleged he purchased with his worthless Western Bond and Mortgage Company Stock, and which he immediately transferred out of his possession for the valuable Western Guaranty Company stock, thereby substituting these securities for the Western Guaranty Company Stock in the coffers of the Western Bond and Mortgage Company, retaining for himself the Western Guaranty Stock. Certainly he should be in a better position to establish the value of these securities and lapse of time should work to his rather than to the Trustee's benefit. But, be that as it may, there was no evidence introduced by or on behalf of Farrington and certainly there is no evidence in the record to establish the fact that the value of these securities would now be difficult to ascertain, or any more difficult than

they would have been within a reasonable time after the trustee discovered or should have discovered Farrington's fraud.

We conclude, therefore, as to the question of laches, that that doctrine has no place in this case—either in law or in fact.

### **DILIGENCE IN PURSUIT OF INFORMATION LEADING TO DISCOVERY**

In his Brief (p. 37) Farrington indicates that a trustee in bankruptcy owes a greater diligence to make discovery than other litigants, and states further:

“If he fails to take proper steps to secure all assets he is presumably negligent and may be charged with the value of the assets lost (re: Reinboth, 157 Fed. 627).”

Later, attention is called to the fact that the Trustee was an attorney, that he held himself out as a tax counselor, that he had the assistance of the Attorney General of the State of Oregon (presumably he meant the deputy Attorney General, Ralph Moody), of the Corporation Department of the State of Oregon, of two auditors of that Department, of Attorney John Latourette and Attorney Sidney Teiser, the latter of whom he generously denominated “one of the ablest bankruptcy attorneys practicing at this bar”, and of Mr. Rudolph Erickson, a certified public accountant, (Appellee's Brief, pp. 40-41) whom he

falsely states "contracted to render services on all phases of the bankruptcy proceedings on a contingent basis." (He neither rendered, nor contracted to render any services on a contingent basis, nor did he contract to render services on *all phases of the bankruptcy proceedings*.)

Now, in light of the fact that a trustee can be charged with the value of assets which he negligently fails to recover for the estate, we ask, first, could McBride, under the facts of this case, be held liable for his failure to recover the assets here charged to have been extracted by Farrington? If not—and we, think the question answers itself—then he should not be chargeable with negligence in the failure to discover.

In view of the fact that McBride, himself, had legal and accounting knowledge, and had all the official and unofficial legal and accounting assistance outlined, we ask, secondly; is not such facts in themselves conclusive of the truth that he was not negligent in his efforts at discovery? On the other hand, does it not compellingly indicate that the truth was so shrewdly and deeply hidden in the books and otherwise by Farrington that it defied discovery by so many experts so long? Ought not McBride be commended for his zeal, and for ultimate discovery, rather than criticized and the creditors punished for his asserted neglect?

Much of Appellee's Brief, from p. 42 to the end, is taken up with an effort to indicate that the trans-

actions charged against Farrington in the plaintiff's complaint were not fraudulent, rather than in the discussion as to whether or not McBride was derelict in his duty to discover.

Much also of the Brief is taken up with a discussion of the postulate propounded by appellee that the whole question of the fraudulent character of the transactions is a question of the value of assets given and received. From which it is argued that since the accountant made no appraisal of the assets the Western Bond and Mortgage Company received, the Trustee was guilty of negligence.

For pages and pages of his Brief Appellee seems to forget that it is the trustee whom he must attack for the so-called lack of diligence, and not the Certified Public Accountant for his asserted inaptness or worse. We maintain that there is no evidence in the record of Accountant Erickson's lack of ability or segacity of or his carelessness. But, even if there were, certainly there was no evidence adduced that McBride was negligent in employing Erickson or that any information was brought home to him of Erickson's suggested unworthiness. Certainly McBride is not chargeable with the failure of the expert accountant to find or to report, if found, facts which should have led to discovery.

The books of the Bankrupt were punctilliously kept and were available, cries the appellee in his Brief. Further, he says, the books contained the data concerning the fraudulent transactions, and the trans-



actions were on the books to be read by any one who would read. However, the facts are that, to the extent of his ability, the trustee read them, two auditors from the Department of the Corporation Commissioner of the State of Oregon read them, the attorneys surveyed them, they were read by Erickson, a practicing Certified Public Accountant for over twenty years and a former member of the Oregon State Board of Accountancy (Tr. p. 140), and all that these experts and near experts read, did not bring to them the revelation of the fraudulent transactions alleged.

Ah!, says Farrington, but the agent of the United States Department of Internal Revenue discovered knowledge of the facts set forth in McBride's complaint, and if such agent could discover such facts, certainly all these other so-called experts should have done so, laying aside for the moment the fact that the revenue agent had available to him books and records of others to which the trustee's experts would not have available (and this, notwithstanding the statement of Farrington's Brief to the contrary). The trustee certainly is not chargeable with the fact that one man, through superior sleuthing or other abilities discovered a fact and others, presumably of like ability, did not discover such fact, at least in the absence of evidence that those whom the trustee employed were known to him to be incapable. The test is what a prudent man under the circumstances should do, and it is quite obvious that McBride acted prudently in employing what the appellee admits was the best legal talent and certainly in employing capable ac-



counting talent in his search for facts. But, the Appellee would have the Court believe that the trustee was negligent in discovering what the experts he employed could not find with the means available.

Now, we come to another question: What is it that Farrington claims McBride did, or failed to do that charges him with negligence in failure to discover?

The evidence shows that the trustee had available the books of account of the bankrupt. That certain newspaper articles came to the attention of the trustee and of his attorney, Mr. Sidney Teiser, in 1936 (Findings III, Tr. p. 73). These articles referred to certain suits brought against the Western Mortgage Company, as well as by that Company against others and that in one of the suits against the company, Farrington was made a party defendant. In this latter suit (*Brockie v. Western Bond and Mortgage Co., Farrington et als*) charges similar to those here made were contained in the complaint. This suit was dismissed on motion of Brockie. The testimony also showed that there was in existence the Revenue Agent's Report which uncovered the alleged fraud of Farrington, but such report was not in the files and records of the Western Bond and Mortgage Company and a copy of it was not obtained by the trustee until a few months before the institution of this suit. Testimony also showed that the trustee had legal council and accountant council and that he on several occasions caused to be conducted examinations under Section 21(a) of the bankruptcy act. The testimony

likewise showed that the trustee was not aware of what was contained in the revenue agent's report and that the reason that he did not see or obtain a copy of this report was that such copy was not in the files of the Western Bond and Mortgage Company and that there was no particular occasion for the trustee to obtain a copy of it, not knowing or having reason to believe what its contents were until the contest of the tax claim filed by the government became imminent. And the testimony also shows that the trustee was instructed by the referee not to precipitate a contest on the government's claim for taxes by filing objections until monies or assets came into the estate sufficient to make the contest of the government's claim anything but academic, and that monies or assets did not come into the estate sufficient to pay expenses until a few months before the bringing of this suit, when final success resulted from the litigation instituted by the trustee against the Bank of California. This we believe is a fair summary of the evidence and there is no dispute concerning it and no contradictory evidence introduced.

Now, we repeat our question. In the light of these facts, wherein was the trustee negligent in his failure to discover? In addition to what has been stated herein it is claimed by Farrington that the trustee was negligent (1) in failing to follow through on the information obtained, and (2) in failing to obtain the revenue agent's report, for, says Farrington, if the Brockie and other complaints had been read and if the revenue agent's report had been scanned, knowl-

edge resulting in discovery or means of discovery would have come to the trustee when these complaints and this report should have been read. We answer. None of the suits except the Brockie suit against Farrington contains allegations leading to the facts alleged in the trustee's complaint, and that merely contained allegations concerning our first cause of action. The other suit, and there is only one other of them in the record, namely the suit of Thompson v. Western Bond and Mortgage Company, contains no allegation which would lead to a discovery of facts concerning the transactions here complained of. Now the Brockie suit was dismissed on motion of the plaintiff, Brockie, in 1931 (Ex. 71) The dismissal was granted over the protest of Farrington (See Defense Ex. 69) and only upon the payment by Brockie prior to its dismissal of a substantial cost bill including a special Master's fee. Now it is conceded that information as to this suit or of the contents of the complaint therein did not come to the trustee until 1936. For that matter, the trustee was not appointed until December 1934. Consequently, it would have been obvious to the trustee had he made investigation in this suit any time after his appointment that Brockie, notwithstanding his allegations in the complaint, had dismissed the suit and had permitted the statute of limitations to run against it. Under the circumstances we maintain that a perusal of the files in the Brockie suit by the trustee would not have lead to any discovery herein for the trustee would have been, with the exercise of reasonable diligence, fully justified in

concluding that allegations contained therein were untrue or unprovable in the light of the fact that Brockie dismissed on his own motion his suit, even against the protest of Farrington and the other defendants and did nothing thereafter permitting the statute of limitations to run against him.

As to the alleged failure of the trustee to obtain earlier a copy of the revenue agent's report: We vigorously insist that in the exercise of due diligence the trustee was fully justified in his inaction in this regard. Of course, he had no knowledge that the agent's report on which an additional assessment was made would contain charges of fraud against Farrington or anyone else. In fact, he had no knowledge at all as to what it might contain except that it must have contained data justifying the agent to recommend additional assessment of taxes. Moreover, we maintain that when the trustee was instructed by the referee not to proceed with filing objection to the Government's claim for taxes or to attempt a contest thereof until money or property came into the estate with which to pay it, at least in part, that his inaction in obtaining earlier a copy of the agent's report was fully justified and, in that regard he was not negligent and did not fail to act with due diligence.

## MISSTATEMENTS AND ARGUMENTS BASED ON MISSTATEMENTS

There are many mistatements and many argu-

ments based on misstatements or unjustified assumptions contained in the appellee's Brief. We shall not attempt to catalogue or to discuss all of them, but we shall content ourselves with but a few.

For example, it is said at page 39 of appellee's Brief,

" . . . at the time of his appointment and even before, plaintiff knew that Farrington and others were under a cloud of suspicion that he had caused assets of the corporation to be fraudulently disposed of."

There is not one scintilla of evidence in the record that McBride knew any such thing on or before his appointment as trustee. The fact is, the only intimation of fraudulent disposition of assets by Farrington was in a newspaper article, filed in 1936 as an exhibit in the case against the Bank of California, and as a matter of fact, the testimony shows that McBride never actually knew what was in this article, but accepted the chargeability of such knowledge to him because his attorney had cognizance of the article.

Again on page 39 in the Appellee's Brief it is stated:

"Even a cursory examination of the bankrupt's books would have disclosed that shortly prior to the filing of the bankrupt's petition two large transfers of assets had been made (the transfers involved in this case) . . . they were unusual transactions and out of the ordinary course of business and therefore challenged attention and investigation as a matter of course, particu-



larly so because the entries disclosed that the Consolidated Credit Corporation Stock was exchanged for the Keystone stock which was owned by the Western Bond and (Tr. p. 144) Western Guaranty Stock was not transferred for money, but was exchanged for other assets."

These statements are not based on evidence. As a matter of fact, an examination of the books of the Western Bond and Mortgage Company will disclose that the transactions referred to were not unusual or out of the ordinary course of business as conducted by the Western Bond and Mortgage Company. There are multitudes of such transactions throughout its books. (See for some of them, the Revenue Agent's Report—Ex. 59.) Moreover, the entries do not disclose that the Keystone stock which was received for the Consolidated Credit Corporation stock was owned by the Western Bond and Mortgage Company, nor is there any reason why the entries on the books concerning these transactions should have a challenged attention and investigation as a matter of course. The entries merely showed that the Western Bond and Mortgage Company in the one instance was transferring some securities which it held (Western Guaranty Stock) for other securities of equal value. And, in the other instance that it was transferring certain securities which it held for other securities of equal value.

On page 41 of appellee's Brief it is said,

"Mr. Moody, Assistant Attorney General, called upon plaintiff immediately after his appointment. . . . He called his attention to the newspaper



accounts (Tr. p. 194) and the litigations in the state and federal courts charging Farrington with fraudulent transfer of assets including the transactions involved in this case."

And, again, at page 71 in the same connection the same statement is repeated in a changed language, this time as follows:

"The attention of the plaintiff was *specifically directed to these newspaper accounts* by Assistant Attorney General Moody immediately after plaintiff's appointment as receiver and subsequent thereto. Mr. Moody arranged that whenever there were any newspaper accounts pertaining to the affairs of the Western Bond that they were to be clipped and turned over to him and he in turn relayed them to the plaintiff . . . There is a large folder full of newspaper clippings in evidence."

We will quote the testimony of Mr. Moody,

"Q. Did you have any conversation with him respecting any civil or criminal liability that might attach to Mr. Farrington in respect to any prosecutions?

A. Well, I told him that he was to look into the matter very carefully and to collect all of the assets that were due. The corporation had created a lot of subsidiary corporations and I asked him to particularly look into that thing and to collect—to find out all of the assets that were due the company.

I remember at one particular time there was The Bank of California matter and I understand that since they have had some judgment.

Q. I want to direct your attention particularly—

A. Oh, yes. Then, as far as Mr. Farrington was concerned, I know I called Mr. McBride's attention to the fact, I think, that Mr. Farrington

ton was interested in the original organization of the Western Bond and Mortgage Company, and the records showed that when they first made application to the corporation commissioner for a license to sell these securities he refused it, whereupon he proceeded to institute in the Circuit Court of the state—to apply for a mandamus compelling the corporation commissioner to accept their filing.

Q. Did you have any discussion with him respecting the lawsuits that had been brought in 1931, charging Mr. Farrington with having defrauded the company?

A. Well, there were some articles published in the newspaper at that time. The newspapers gave a great deal of publicity to this whole business, this whole transaction, and I was watching it very closely, and whenever there was some reference to some proceeding about Mr. Farrington, that was called to Mr. McBride's attention.

Q. By you? A. Yes. (Tr. 193-194)

(Cross Examination)

Q. You spoke of some papers, some articles being published in the newspapers and, that you saw the articles because you were interested. That was in 1934 that you are speaking of, articles appearing in the papers of 1934, is that right?

A. In answer to that, I wanted to say that I was quite interested in the case. It was a live case for me, and it had been assigned to me, and there was considerable publicity about the State intervening, and there was also considerable publicity in regard to the Western Bond and Mortgage Company, and I instructed all of them that whenever any article appeared in the paper about that to call my attention to it and, while I do not mean to say that I have any independent recollection about reading any article, I know whenever I did I came to Portland and spent

several days at a time talking to Mr. McBride, and his attention was always called to these things.

Q. What I am speaking about is that you referred to newspaper articles published concerning matters which had occurred after you became interested in the bankruptcy proceedings.

A. Yes, after I became interested.

Q. And not before 1934?

A. I, myself, knew nothing about the Western Bond and Mortgage Company until it was referred to me some time in 1934." (Tr. 199-200)

That is all the testimony of Mr. Moody on the subject, and it certainly does not bear out statements quoted from appellee's Brief. We particularly call attention of the Court to the fact that the newspaper articles referring to the Brockie suit (Ex. 64, 65 and 84—pp. 31, 32 and 84 of Appellee's Appendix of Exhibits), the Thompson suit (Ex. 75—p. 64 Appellee's Appendix), and the Pape suit (Ex. 85—p. 81 of Appellee's Appendix), *all appeared in the newspapers in 1931*. The only newspaper articles appearing in 1934 were articles concerning the bankruptcy cause itself. (See exhibits 78, 79, 80, 81, 82 and 83—pp. 69, 71, 74, 76, 77 and 78, Appellee's Appendix). So obviously the newspaper articles to which Mr. Moody called the Trustee's attention were not those concerning the suits to recover property fraudulently received by Farrington. Such articles appeared in 1931, three years previous.

Again on page 53 of the Appellee's Brief it is stated:

"The (Revenue Agent's) report is dated October

12, 1932, and it recites (p. 1) that the information contained in the report was obtained from '*an examination of the books and records of above named affiliated group.*' A reading of the report confirms the fact that it purports to show *only what is in the books.*"

The Revenue Agent's report specifically indicates that there was an examination of the books of other companies than the Western Bond and Mortgage Company. For example, on page 2 of the report as copied into Appellee's Appendix of Exhibits it is said;

"These transactions were reflected on taxpayers books *and upon the books of the Consolidated Credit Corporation* by a series of complicated book entries, and it was necessary to spend several days in analyzing the entries on the books of both companies to determine just what took place.

On page 3 of the agent's report, as reproduced in the Appellee's Appendix of Exhibits, it is stated:

"The Consolidated Credit Corporation purchased the 150 shares of outstanding stock of the Consolidated Credit Company from the Western Bond and Mortgage Company, at a purported price of \$75,000.00. This transaction was reflected on *its* books by the following entry."

and the entry indicates clearly that it was an entry *on the Consolidated Credit Company books.*

On page 9 of the Report, as reproduced in Appellee's Appendix of Exhibits, it is stated:

"The tax liability accruing to the Laurel Invest-

ment Company on this deal is being covered in a separate report on that company."

Obviously the revenue agent had to make an examination of the Laurel Investment Company books in order to make a report on that company.

The record itself, therefore, patently denies the statement made by Appellee in his brief that a reading of the report confirms the fact that it purports to show only what is in The Western Bond and Mortgage Company's books. It shows expressly that an examination of books of other companies were made.

The statement taken by appellant from the heading of the report, that,

"An examination of the books and records of the above-named affiliated group for the calendar year 1930, disclosed the following in connection with its income tax liability"

was obviously not intended to be a statement that only the books of the taxpayer were being examined.

We shall desist from detailing other examples.

## CONCLUSIONS

We assert therefore, that the evidence of record in this proceeding cannot justify the holding by the trial court that the trustee failed to exercise due diligence in earlier discovering the fraud of Farrington, set forth in the transactions alleged in his complaint.

We assert further that none of the derelictions



charged against the trustee applies to the second claim, viz., the transaction concerning the transfer out of the Western Bond and Mortgage Company of forty thousand shares of the Consolidated Credit Corporation stock for property already owned by the Western Bond and Mortgage Company.

We urgently insist that this case should be reversed and the cause remanded for trial on the question of fraud.

Respectfully submitted,

SIDNEY TEISER,

W. G. KELLER,

(Teiser & Keller)

Attorneys for Appellant.



In the United States  
**Circuit Court of Appeals**  
For the Ninth Circuit

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GEORGE M. McBRIDE, Trustee in Bankruptcy  
of Western Bond and Mortgage Company, an  
Oregon Corporation, Bankrupt,  
*Appellant,*

v.

C. H. FARRINGTON,  
*Appellee.*

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Upon Appeal from the District Court of the United  
States for the District of Oregon.

---

**APPELLANT'S REPLY TO APPELLEE'S  
SUPPLEMENTAL MEMORANDUM**

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**FILED**

JUN 19 1946

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**PAUL P. O'BRIEN,**

**CLERK**



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---

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SUPPLEMENTAL MEMORANDUM**

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The Appellee saw fit to file and serve, on the day of the argument of this case, a Supplemental Memorandum claiming that the Appellant had advanced for the first time certain arguments in his Reply Brief. This was obviously not correct because the points covered by the Appellee's Supplemental Memorandum were points which were raised by Ap-

pellee in his brief, and were therefore answered by Appellant in his Reply Brief. There was no new matter in our Reply Brief. It contained merely a refutation of arguments made by the Appellee in his Brief.

However, be that as it may, the first point stressed by Appellee in his Supplemental Memorandum is that Findings of Fact III made by the trial court, that,

“Plaintiff had actual knowledge *or* was in possession of information which was sufficient to guide him to actual knowledge of the matters alleged in the complaint,”

was a proper finding of fact. Since Appellee in its Brief claimed this finding (as well as others) was not subject to review, we had insisted that such finding was reviewable because it was not a real finding of fact and was meaningless as a finding. That is was a mere argument, a conclusion, or at best an inference. A finding, we maintained, and still maintain, must be a finding *of fact* and certainly a court cannot properly make a finding in the form of “either/or.” If the facts had justified a finding that actual discovery had been made, then a finding to that effect should have been made. If, on the other hand, the court found that there were facts presented in evidence which justified the conclusion that the trustee was in possession of information which was sufficient to guide him to knowledge, then the finding should have set forth



specifically what such facts were. We presented this view to the court in our Reply Brief, as a demonstration that the findings of the trial court were merely inferences or conclusions and not really findings, and we, therefore, asserted that this court was as capable of making such inferences and conclusions as was the trial court, since it had all the evidence before it and there was no dispute concerning the testimony nor any contradictions therein.

We insist that the three cases cited and quoted from by the Appellee in his Supplemental Memorandum (pp. 2 to 4) do not bear out what it is claimed for them by Appellee.

*Clyde Equipment Co. v. Fiorita*, 16 F. (2d) 106, has no bearing whatsoever on the propriety or impropriety of a disjunctive finding. It merely holds that a finding susceptible of one of two constructions will be given the construction which will support the judgment. Obviously that is good law, but it has no applicability here.

*Perkes v. Utah Idaho Milk Co.*, (Utah) 39 P. (2d) 308, 311, merely holds that findings made in the alternative, both of which may be true, do not in themselves justify a *reversal* of the judgment. (See Syllabus 8). We have never claimed that Finding No. III was of such a nature as to justify a reversal. All that we maintained was that the finding was of such a nature as to impel the appellate court to treat it as a mere inference or conclusion, and not as a real finding of *fact*. Therefore, we insisted that the ap-

pellate court was as well qualified as the trial court to make its own inferences, since the evidence was not conflicting.

*Rubenstein v. Washington Cold Storage Co.*, (Wash.) 138 P. (2d) 852 (incorrectly cited by Appellee as 148 P. (2d) ), merely held that a finding that loss of whiskey in a warehouse was caused either by theft or leakage and through no negligence of the warehouseman supported a judgment in favor of the warehouseman. Obviously such a holding was proper since the question for determination was merely the negligence or care of the warehouseman.

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The attempt by Appellee (pp. 3-4) to insinuate that the testimony of McBride, to the effect that he had no knowledge of the acts charged in the complaint until shortly before suit was instituted, should be given no weight, and the citation of *Foster v. Mansfield C. & L. M. Co.* 13 Sup. Ct. 28, 146 U.S. 88, 36 L. Ed. 899, as justifying such insinuation, is without warrant. We agree with the statement in that case that the defense of want of knowledge is easily made and easily testified to by one claiming such want, but we find nothing in that case to indicate that where such testimony is positively given and where there is no evidence to the contrary that a finding of knowledge may be supported without any evidence on which to base it, as against contrary positive testimony.

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Appellee next maintains in his Supplemental Memorandum (pp. 5-9) that the court was justified in finding that the participants in the transaction who had died, knew the material facts and that therefore defendant was deprived of the means of his defense through inability to produce evidence. He claims that *mere death alone* or a *likelihood* that there would be an obscuration or loss of evidence by a lapse of time justifies the finding of laches by a trial court, even though there be no testimony showing such a loss or obscuration or a showing that those who had died had knowledge of material facts helpful to defendant. The Appellee cites an authority (30 C.J.S., Section 119, page 543) and several cases. However, a reading of this authority and of these cases do not justify any such conclusion. In fact, the very authority cited by the appellee states,

“Death of a party will not alone render doctrine of laches applicable, and loss of evidence, although affording test of applicability of laches, must be material. *Shirley v. Van Every*, 167 S.E. 345, 159 Va. 732; 21 C.J., p. 236 note 1 (b); C.J.S., §119, p. 543, note 35.”

Further the very next section in C.J.S. (Section 120, pp. 543-544) says,

“Lapse of time will not bar relief where circumstances exist which excuse the delay and render it inequitable to interpose the bar. To charge a party with laches in delaying to assert a right, an opportunity to have acted sooner must have existed; if he acted at the first opportunity, and sued substantially as soon as the occasion arose

for an assertion of his right, laches are not imputable to him. . . . Greater liberality is allowed in excusing delay where actual fraud is charged than in other cases. The criterion of what constitutes an excuse is applied with less strictness where plaintiff is a *public officer* seeking to enforce public rights than where he sues as an individual." (*Emphasis ours*)

Moreover, the Oregon cases are to the contrary.

In *Willis v. Nehalem Coal Co.*, 52 Ore. 70, 89; 56 P. 528, it is said,

"It is asserted by defendants that the complaint shows that for fully four years prior to the institution of this suit plaintiff had full notice and knowledge of the grievances complained of, and from this it is argued that they are guilty of such laches that must defeat the suit. *Full knowledge of all the facts* concurring with a delay for an unreasonable length of time are the essential elements of the defense of laches. Until *knowledge* is shown to exist, the beginning of time from which laches will run cannot be said to commence: 2 Cook, Corporations (4th Ed) 771 . . . . The rule, if such is the rule, that, when the means or knowledge are open to the stockholder, he is chargeable with knowledge from the date when he should have ascertained the facts, cannot be applied here for two reasons: First, because the means of knowledge is rebutted by the averment, that the officers and directors have refused to permit the stockholders to examine the books of the corporation: and, second, because *constructive notice or knowledge does not apply to a case of fraud and cannot relieve a party responsible for fraud.*" (*Emphasis ours*)

In the case of *May v. Roberts*, 133 Ore. 643, 659; 286 P. 546, it is held,

"Mere delay of itself is not laches, *but delay that has worked to the injury of another*. . . . The defendants contend that valuable evidence in support of their case was lost by the death of Robert Gunning, . . . that if he were alive he would testify to his own good faith in the proceedings. . . . The fraud and collusion of defendant and associates . . . is conclusively established by their own evidence. The testimony of Robert Gunning would not be of any avail to them: *Sedlak v. Sedlak*, 14 Or. 540 (13 P. 452)." (*Emphasis ours*)

In *American Surety Co. v. Multnomah County*, 171 Ore. 287, 327; 138 P. (2d) 597, it is said,

"We find nothing in the complaint other than the apparent lapse of time which is suggestive of laches. Lapse of time does not constitute laches *unless the delay works to the injury of another*. *Wills v. Nehalem Coal Company*, 52 Or. 70, 56 P. 528; *May v. Roberts*, 133 Or. 643, 286 Pac. 546. It has also been held that *full knowledge of all the facts* concurring with a delay for an unreasonable time are essential elements of the defense of laches, and we are not bound to presume that Marion County or the plaintiff surety company had knowledge of Drager's defalcations. *Wills v. Nehalem Coal Company*, *supra*." (*Emphasis ours*)

From these Oregon cases it will be observed that there is a definite requirement that the evidence must show that the delay has worked to the injury of the party claiming laches and therefore, it must show that the facts, which death caused an inability to pro-



duce, would have been favorable to the party asserting laches, for otherwise, the delay could not be to his injury. The record of this case as has been pointed out in our previous Brief, makes no such showing.

It will also be observed from the Oregon cases and from the authority here cited, that where laches are charged against an officer seeking to enforce rights of others the doctrine will be applied with less strictness than in other causes (30 C.J.S. Section 120, p. 543), and that likewise *in cases of fraud, constructive knowledge will not apply.* (Wills v. Nehalem Coal Co. and American Surety Co. v. Multnomah County, ante).

Thus, we return to what was said on behalf of Appellant in the argument: Where a trustee in bankruptcy is charged with laches in a case where fraud is asserted, there should be no severe strictness in measuring the alleged delinquencies of the trustee as against the fraudulent activities of the defendant. Certainly, deliberate and secretive fraud is more vicious than mere asserted carelessness or negligence. Certainly too, consideration should be given to the fact that a trustee represents creditors and that these creditors are to gain by his successful activities and to lose by his failure, whatever the cause of such failure may be. Yet such creditors have no control over the trustee as such and are not to be charged as principals of the trustee in the normal legal sense. We therefore again assert, that there should be no nice balancing of the scales in order to invoke the



doctrine of limitations or of laches in the favor of a defrauding party as against innocent creditors who have been injured by the fraud.

Respectfully submitted,

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Attorneys for Appellant.



No. 11140

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United States  
Circuit Court of Appeals  
For the Ninth Circuit.

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BERNARD G. SHEPHERD,

Appellant,

vs.

MILDRED McDONALD, now MILDRED MUCK,  
Appellee.

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Transcript of Record

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Upon Appeal from the District Court of the United States  
for the District of Oregon

FILED

APR 25 1945

PAUL P. O'BRIEN,  
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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In the District Court of the United States  
for the District of Oregon

No. B-26580

In the Matter of  
BERNARD G. SHEPHERD,  
Bankrupt.

Certificate of Referee on Petition of Bankrupt  
for Review of Referee's Order Qualifying  
Bankrupt's Discharge by Excluding the Debt  
of Mildred Muck, Objecting Creditor

To the Honorable James Alger Fee and Claude  
McColloch, Judges of the Above Entitled  
Court:

Estes Snedecor, the referee in bankruptcy in charge of this proceeding, hereby makes this his certificate on the petition of Bernard G. Shepherd, bankrupt herein, for a review of the referee's order entered March 3, 1945, which qualified the discharge of the bankrupt by excepting from the operation of the discharge the debt owing to Mildred McDonald, now Mildred Muck, on which the bankrupt had waived a discharge obtained in a former bankruptcy.

### QUESTIONS PRESENTED

In a last analysis, the only question presented is whether a bankrupt, after having obtained a discharge from a debt in a prior proceeding and having revived the debt by waiving his discharge, may receive another discharge, over the objection



of the creditor, from the same debt in a new proceeding brought more than six years after the first discharge. Reference is made to the petition for review for a statement of the particulars in which it is claimed the referee erred in denying the bankrupt a discharge from the particular debt mentioned.

### FACTS

The facts are undisputed and are set forth on pages 2 and 3 of the referee's opinion. Inasmuch as the facts involved in the particular issue before the court are not disputed and are matters of record in this court and in the Circuit Court of the State of Oregon for the County of Multnomah, it is deemed unnecessary to transcribe and certify the testimony taken before the referee. [1\*]

### PAPERS SUBMITTED

Transmitted herewith are the following papers:

1. Specifications of Objections to Discharge and Petition for Refusal, filed May 4, 1942.
2. Amended Specifications of Objections to Discharge and Petition for Refusal, filed August 7, 1944.
3. Motion to Strike Third Specification of Objection and Order Denying Motion, filed August 7, 1944.
4. Order Denying Leave to File Amended Specifications of Objection to Discharge, entered August 25, 1944.

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\* Page numbering appearing at foot of page of original Reporter's Transcript.

5. Order Denying First and Second Specifications of Objection to Bankrupt's Discharge and Taking under Advisement the Third Specification, entered August 28, 1944.

6. Objector's Exhibits 1 and 2, and Bankrupt's Exhibits 6 and 7.

7. Referee's Opinion, filed March 3, 1945.

8. Qualified Discharge of Bankrupt, original of which is already on file with the clerk of this court.

9. Bankrupt's Petition for Review of Referee's Order Qualifying the Discharge of the Bankrupt, filed March 7, 1945.

Dated at Portland, Oregon, this 7th day of March, 1945.

Respectfully submitted,

ESTES SNEDECOR

Referee in Bankruptcy

[Endorsed]: Filed March 7, 1945. Estes Snedecor, Referee in Bankruptcy.

[Endorsed]: Filed March 7, 1945. Lowell Mundorff, Clerk. [2]

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i[Title of District Court and Cause.]

SPECIFICATIONS OF OBJECTIONS TO DIS-  
CHARGE AND PETITION FOR REFUSAL

Mildred Muck, formerly Mildred McDonald, in the County of Multnomah, in the State of Oregon, a Creditor of said bankrupt, does hereby oppose the granting to said Bernard G. Shepherd of a dis-

charge from his debts; and for the grounds of such opposition does file the following specifications:

### FIRST SPECIFICATION

That on or about the 16th day of December, 1941, whilst a bankrupt and after the appointment and qualification of a trustee, George P. Clark, the above named bankrupt knowingly and fraudulently concealed the following assets belonging to the estate from said trustee, to-wit: one 1941 Cadillac sedan automobile motor No. 6341044 bearing Oregon license No. 152-613 for the year 1942; one man's ring with a large diamond setting, and all of his interest in all of the property, real and personal, left by Tho. H. Shepard, who died in the State of Alabama in 1933, which estate was left by will dated January 10, 1933, whereby the said Tho. H. Shepard left all of his estate to Nannie Shepard to have and to hold during her life or widowhood and upon her remarriage or upon her death all of his property to be divided equally between Bernard Shepard (Shepherd), this bankrupt, and Lewis Shepard, share and share alike. That said automobile and diamond ring at the time of the appointment and qualification of the trustee herein were being held on secret trust by Mary Shepherd, wife of the bankrupt.

Said bankrupt knowingly and fraudulently omitted all of said property from his schedule of assets herein, and failed to reveal to said trustee the existence of the same or the facts as to the title [3] thereto and fraudulently and knowingly con-

ceased said property, so as aforesaid belonging to his estate, whilst such bankrupt, from his said trustee.

## SECOND SPECIFICATION

That on or about the 16th day of December, 1942, in this bankruptcy proceedings, Bernard G. Shepherd, the bankrupt herein, knowingly and fraudulently made a false oath in relation to said proceedings in bankruptcy, as follows, to-wit: said bankrupt omitted the following property from his schedule and yet did then and there knowingly and fraudulently make oath to said schedules that they were a true statement of his assets and that after being duly sworn on general examination stated that he never at any time signed any statement to the effect that he was the owner of any automobile since 1931, including the 1938 Cadillac sedan automobile heretofore mentioned herein. That he was not the owner of said 1941 Cadillac sedan, and that he had assigned his interest in and to all of his share of the estate to Tho. H. Shepard, deceased, whereas in truth and in fact as said bankrupt well knew, he had signed a bill of sale stating that he was the legal owner of said 1938 Cadillac automobile and had a right to sell same and whereas, in truth and in fact as said bankrupt well knew, he had made no legal transfer of his interest in said estate of Tho. H. Shepard, deceased. Said testimony was material and it pertained to the discovery of the acts, conduct and property of the bankrupt in that said property

so admitted and testified to was and is his property and was of value.

### THIRD SPECIFICATION

Heretofore and on the 27th day of June 1931, the bankrupt herein was duly adjudged a bankrupt in the District Court of the United States for the District of Oregon in proceeding No. B-16240 closing file No. 15751, which cause was thereupon duly referred to the Honorable A. M. Cannon, referee and in which proceeding the bankrupt was thereafter on the 21st day of October, 1931, duly discharged of all of his debts except such as were then by law excepted therefrom. [4]

In his schedule filed in said proceeding No. B-16240 the Bankrupt scheduled in schedule "A" thereof, among other creditors and claims, the following:

Mildred McDonald contract in 1929 re various notes and open account as a partner of Lorenzo Mansfield doing business as Lorenzo-Mansfield Studios—\$2600.00.

The said Mildred McDonald, (now Mildred Muck), named in said schedule "A" as creditor of the bankrupt is the identical individual as the objecting creditor in the instant proceeding. Subsequent to his adjudication in bankruptcy in said proceeding No. B-16240 and subsequent to his discharge the bankrupt promised and agreed to pay to this objecting creditor the claim so scheduled and discharged. Thereafter, and on the 7th day of February, 1935, the Circuit Court of the State



of Oregon, for the County of Multnomah, duly made and entered its judgment according to law upon the verdict of a jury on the prayer of the complaint on this objecting creditor in favor of this creditor and against the bankrupt, that the bankrupt was indebted to this creditor, upon said promise to pay said scheduled and discharged claim in the amount of \$2,543.95, with interest thereon from June 10, 1930 at the rate of 6% per annum and costs taxed in the sum of \$32.25, which said judgment is the judgment referred to and described in schedule "A" in the bankrupt schedule in the instant proceeding.

Said Circuit Court of the State of Oregon, for the County of Multnomah was at all times mentioned herein and is now a Court of general jurisdiction of the State of Oregon and had jurisdiction of the subsequent matter of the action in which said judgment was rendered. In said action the bankrupt appeared personally and by his attorney and submitted his person to the jurisdiction of said court.

This objecting creditor is the only unsecured creditor listed in schedule "A" of the Bankrupt's schedules herein.

Said judgment is the identical claim discharged in said [5] proceeding No. B-16240, which said discharge has been waived by the bankrupt, and the bankrupt cannot again seek nor secure a discharge of said claim.

MILDRED MUCK

Claimant



State of Oregon,  
County of Multnomah—ss.

I, Mildred Muck, being first duly sworn, depose and say: That I am the claimant in the above entitled matter; that I have read the foregoing petition, know the contents thereof and believe the same to be true.

MILDRED MUCK

Subscribed and sworn to before me this 4th day of May, 1942.

[Seal]

JOHN D. GALEY

Notary Public for Oregon

My Commission Expires March 20, 1943.

State of Oregon,  
County of Multnomah—ss.

Due and legal service of the foregoing objections is hereby admitted in Multnomah County, Oregon, this 4 day of May 1942.

PAUL M. LONG

Of Attorneys for Bankrupt

[Endorsed]: Filed May 4, 1942. Estes Snedecor, Referee in Bankruptcy.

[Endorsed]: Filed March 7, 1945. Lowell Munderff, Clerk. [6]

[Title of District Court and Cause.]

MOTION TO STRIKE THIRD SPECIFICA-  
TION OF OBJECTION AND ORDER  
DENYING MOTION

Comes now Bernard G. Shepherd, the above named bankrupt, and moves this Court to strike the third specification of objection filed herein to the bankrupt's discharge on the ground and for the reason that said third specification does not state any facts sufficient to support or permit the granting of an order denying a discharge to the bankrupt in this proceeding.

COAN & ROSENBERG

Of Attorneys for Bernard G.  
Shepherd, Bankrupt

This motion having come on for hearing before the undersigned Referee on August 7, 1944, and the court having considered argument of counsel,

It Is Ordered that the foregoing motion be denied.

ESTES SNEDECOR

Referee in Bankruptcy

[Endorsed]: Filed August 7, 1944. Estes Snedecor, Referee in Bankruptcy.

[Endorsed]: Filed March 7, 1945. Lowell Mundorff, Clerk. [7]

[Title of District Court and Cause.]

ORDER DENYING FIRST AND SECOND  
SPECIFICATIONS OF OBJECTION TO  
BANKRUPT'S DISCHARGE

This Court having set for hearing the specifications of objection to the bankrupt's discharge on the 7th day of August, 1944 at the hour of 2:00 P. M., at the court room of this court, the United States Courthouse, Portland, Oregon, the objecting creditor, Mildred Muck appearing in person and by and through her attorney, W. E. Richardson, and the bankrupt appearing in person and by and through his attorney, Ralph A. Coan, and the Court, having heard the testimony of the objecting creditor in support of said specifications of objection, and the evidence offered by the bankrupt in opposition thereto, finds:

That there is no evidence in support of specification one and two, designated as first and second specification of objection, and;

It Is Therefore Ordered that the first and second specification of objection be and the same are hereby denied, disallowed and overruled.

It Is Further Ordered that the Court does take under advisement the third specification of objection.

ESTES SNEDECOR

Referee

Dated this 28th day of August, 1944.

[Endorsed]: Filed August 28, 1944. Estes Snedecor, Referee in Bankruptcy.

[Endorsed]: Filed March 7, 1945. Lowell Mundorff, Clerk. [8]

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[Title of District Court and Cause.]

### REFEREE'S OPINION

This cause came on for hearing August 7, 1944, upon specifications of objection of Mildred Muck, a creditor, to the discharge of the bankrupt. Each appeared in person and by counsel. At the outset, the objecting creditor presented and asked leave to file amended specifications. The bankrupt moved to strike the third specification as originally filed.

The amended specifications consisted of a reiteration of the original three specifications and a new one designated "Fourth Specification". The latter contained allegations of fact not mentioned in the original specifications and constituted an attempt to set up a new and additional ground for the denial of bankrupt's discharge. The time for filing specifications had long since expired. The referee denied the motion for leave to file the amended

specifications. Collier on Bankruptcy, 14th Ed. Section 14.07, Page 1276; In re Johnson (D. C., S. D.) 192 Fed. 356, 27 A.B.R. 644; In re Hurowitz (D. C. Mass.) 14 F. Supp. 71, 28 A.B.R. (N. S.) 479; In re Gagliardi (D. C. N. Y.) 36 A.B.R. (N.S.) 326; Northeastern Real Estate Corporation v. Goldstein, 91 F. (2d) 942, 34 A.B.R. (N. S.) 652; In re Martina (D. C. N. Y.) 47 A.B.R. (N.S.) 182.

The referee also denied bankrupt's motion to strike the third specification. Reasons for the latter ruling will be discussed later.

After hearing the testimony and considering the evidence offered in support of the first and second specifications the referee ruled in open court that there was no competent evidence to sustain [9] the allegations. Thereafter an order was entered denying and overruling the first two specifications of objection.

The referee took under advisement the third specification and requested briefs; which now have been duly considered.

The third specification raises a question of first impression under the Bankruptcy Act. The question is, may the bankrupt, after having obtained a discharge from a debt in a prior proceeding and having revived the debt by waiving his discharge, receive another discharge from the same debt in a new proceeding brought more than six years after the first discharge.

The undisputed facts are: The bankrupt was duly adjudged a bankrupt upon a voluntary petition filed June 26, 1931. Thereafter on October 21, 1931, he

was granted a discharge. (Bankrupt's Petition 6). He listed as one of his creditors Mildred McDonald, now Mildred Muck, the objecting creditor herein. The bankruptcy schedules show that the bankrupt was indebted to this creditor on notes signed by him in the sum of approximately \$2600. (Bankrupt's Exhibit 7).

On June 5, 1934, Mildred Muck brought an action in the Circuit Court of the State of Oregon against the bankrupt to recover the amounts owing on said promissory notes. The defendant answered by admitting that he was indebted in the amount alleged but, as an affirmative defense, set up his discharge in bankruptcy. The plaintiff in her reply admitted the discharge, but alleged affirmatively that after the bankrupt had filed his petition in bankruptcy and prior to his discharge, he had expressly promised and agreed to pay the notes; that he had stated that he had listed her as a creditor because he was required to do so, but that she could disregard the bankruptcy. She alleged further that pursuant to the agreement he had paid certain sums on account thereof before and after his discharge. A jury trial upon these issues resulted in a verdict and judgment thereon, entered August 7, 1935, for the full amount then [10] owing on said notes in the sum of \$2543.95 with interest thereon at the rate of 6% per annum and costs.

On December 16, 1941, Bernard G. Shepherd filed a second bankruptcy proceeding in which the only unsecured creditor listed is Mildred Muck, the objecting creditor. In her third specification,



the objecting creditor set forth substantially the foregoing facts and stated that her claim evidenced by the judgment based upon the bankrupt's promissory notes is the same obligation from which the bankrupt received a discharge in the former proceeding. She contends that the bankrupt having once waived the right to a discharge in bankruptcy on a debt cannot have another discharge on the same debt.

Neither counsel nor the referee has been able to find a reported case precisely in point. In searching for an analogous situation we find a long list of authorities holding without exception that where a bankrupt, prior to the Chandler Act, failed to apply for a discharge or to pay the costs of the proceedings thereon, he is forever barred from a discharge on the same debts in a subsequent proceeding. *Kuntz v. Young* (C.C.A. 8th) 131 Fed. 719, 12 A.B.R. 505; *In re Kuffler* (C.C.A. 2nd) 151 Fed. 12, A.B.R. 16; *Pollet v. Cosel* (C.C.A. 1st) 179 Fed. 488, 30 L.R.A. (N.S.) 1164, 24 A.B.R. 678; *In re Loughran* (C.C.A. 3rd) 218 Fed. 619, 33 A.B.R. 350; *Hill v. R. R. Industrial Finance Co.* (C.C.A. 10th) 92 F. (2d) 973, 35 A.B.R. (N.S.) 304; *In re Bacon* (C.C.A. 5th) 193 Fed. 34, 27 A.B.R. 737; *Horner v. Hamner* (C.C.A. 4th) 249 Fed. 134, 40 A.B.R. 817; *In re Schwartz* (C.C.A. 2d) 89 F. (2d) 172, 33 A.B.R. (N.S.) 673; *Perlman v. 322 West 72nd Street Co., Inc.*, (C.C.A. 2d) 127 F. (2d) 716, 49 A.B.R. (N.S.) 212; *People's Loan and Savings Company v. Charles Emmett Dowdle* (C.C.A. 5th) 92 F. (2d) 442, 34 A.B.R.

(N.S.) 747; Colwell v. Epstein (C.C.A. 1st) 142 F. (2d) 138, 56 A.B.R. (N.S.) 97; Freshman v. Atkins, 269 U. S. 121, 123, 46 S. Ct. 41, 70 L. Ed. 193, 6 A.B.R. (N.S.) 744; Collier on Bankruptcy Par. 14.05, p.p. 1262-1264.

The reasoning employed in most of these cases is well summarized [11] in a recent decision of the United States Circuit Court of Appeals, First Circuit, as follows: "The reasons given for those decisions were the time limitation in the statute itself and the doctrine of *res judicata*. In them the courts pointed out that to grant a discharge in the second proceeding from debts provable in the earlier proceeding where no application for discharge had been made, would empower the bankrupt effectively to evade the statutory limitation and place within his control the time when he should act. This would operate as an enlargement of the time limit prescribed in the statute and would interfere with the speedy administration of the bankrupt estate. It would be contrary to the spirit and purpose of the statute. They also said that where the bankrupt fails to petition for a discharge the result is in effect a judgment by default in favor of his creditors that he was not entitled to a discharge from their claims. Such a judgment is as forceful as a judgment after trial and is conclusively *res judicata* between him and the creditors whose claims are listed in the bankruptcy schedules. The result is that the issue presented in the second petition is the same as that which existed in the first and which had been decided against him

and in favor of his creditors." *Colwell v. Epstein et al.*, 142 F. (2d) 138, 56 A.B.R. (N.S.) 97.

The courts have adhered strictly to this rule no matter how extenuating the circumstances may have been that caused the bankrupt to fail or neglect to prosecute his initial proceeding for a discharge. It is not an exaggeration to state that nearly all such defaults were the result of carelessness upon the part of counsel or the bankrupt occasioned in turn by an utter lack of appreciation of the final consequences of their inaction or indifference. A number of decisions stress the point that the only object of a bankruptcy proceeding in a no asset case is to obtain a discharge. If a bankrupt fails to prosecute the proceeding, he is barred from bringing another proceeding for a discharge of the same debts. Such a course amounts [12] to an abuse of the process of the court and will not be countenanced. In *re Fiegenbaum* (C.C.A. 2nd) 121 Fed. 69, 9 A.B.R. 595; *Freshman v. Atkins*, *supra*; In *re Vardell* (D.C. Tenn.) 28 A.B.R. (N.S.) 697; *Perlman v. 322 West 72nd Street Co., Inc.*, *supra*.

If such is the attitude of the courts toward a bankrupt who is indifferent to the relief available to him under the Act, should we expect them to assume a different attitude toward a bankrupt who obtains full relief under the Act and simultaneously waives his discharge on a particular debt? Does it not logically follow that having waived the benefits of the Act as to a particular debt he cannot again seek relief from the same obligation? "It is the purpose of the Bankruptcy Act to convert

the assets of a bankrupt into cash for distribution among his creditors, and then to relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes." *Williams v. U. S. Fidelity Co.*, 236 U. S. 549, 35 S. Ct. 289, 59 L. Ed. 713, 34 A.B.R. 181.

In the case before us the bankrupt was accorded full relief in the first bankruptcy from oppressive obligations resulting from business misfortunes. Having waived his right to relief from a particular debt, he is forever barred from seeking again like relief from the same obligation.

The bankrupt, by his motion to strike the third specification, contends that he is entitled to a discharge from all his provable debts unless the specification invokes one of the causes for a denial of a discharge as defined in Section 14c of the Act. It has long been the recognized practice of the bankruptcy court, upon motion of a proper party, or on its motion if the facts appear from its records, to qualify a discharge by excluding debts on which the bankrupt is barred from obtaining relief. *Bluthenthal v. Jones*, 208 U. S. 64, 52 L. Ed. 390, 19 A.B.R. 288; *In re Zeiler* (D.C. N.Y.) 18 F. Supp. 539, 33 A.B.R. (N.S.) 627; *In re Epstein* (D.C. Cal.) 12 F. Supp. [13] 450, 27 A.B.R. (N.S.) 319; *In re Summer* (C.C.A. 2nd) 107 F. (2d) 396, 41 A.B.R. (N.S.) 246; cert. den. 309 U. S. 680, 60 S. Ct. 718, 84 L. Ed. 1024; *In re Early* (E.D. Pa.) 34 F. Supp. 774, 43 A.B.R. (N.S.) 518; *In re*

Tucker (E.D. N.Y.) 49 F. Supp. 239, 53 A.B.R. (N.S.) 106.

In Collier on Bankruptcy, 14th Edition, Par. 14.62, p. 1381, 1944 Supplement, it is stated: "This practice represents in effect the sole exception to the well settled general rule that a bankruptcy court will not determine the dischargeability of individual claims, and that such questions must be litigated in other appropriate forums when the discharge is pleaded as a defense."

This case falls within the exception. The specifications goes farther than to point out a ground for the denial of a discharge. It challenges the bankrupt's right to any relief as to the particular debt. It draws the court's attention to the fact that the bankrupt had previously obtained relief under the Bankruptcy Act from the debt and had expressly waived all rights under the Act. In cases where it appeared that all debts scheduled were listed in a prior proceeding in which the bankrupt failed to obtain a discharge, the court dismissed the second proceeding or denied the discharge altogether. In *re Stone* (D.C. Oregon) 174 Fed. 947, 23 A.B.R. 24; *Perlman v. 322 West 72nd Street Co., Inc.*, *supra*; *Kuntz v. Young*, *supra*. In cases where the bankrupt had incurred new liabilities since his first proceeding, his discharge was qualified by excepting the debts listed in the former proceeding. In *re Loughran*, *supra*; In *re Summer*, *supra*; In *re Zeiler*, *supra*; In *re Brown* (D.C. N.H.) 35 F. Supp. 619, 47 A.B.R. (N.S.) 539. In the case before us the bankrupt listed only the



one unsecured creditor, but scheduled another creditor holding a note and mortgage on real property which he signed with his wife in 1941. Presumably he is entitled to a discharge from personal liability on the mortgage debt. Accordingly the proper procedure is to enter a qualified discharge, excepting the debt of the objecting creditor as undischageable. [14]

Counsel for the bankrupt argues with much force that the promise to pay the discharged debt creates an entirely new and distinct obligation which is dischargeable in a subsequent bankruptcy. He cites a recent decision of the United States District Court (Western District of Kentucky) 33 Fed. Supp. 976, 47 A.B.R. (N.S.) 668, in which the Court said: "The present case is therefore subject to the well settled rule that a discharge in bankruptcy, while releasing the bankrupt from liability to pay a debt that was provable in bankruptcy, leaves him under a moral obligation sufficient to support a new promise to pay the debt, regardless of whether the new promise was made before or after the discharge in bankruptcy. Posey v. Mayer's Adm'r, 3 Ky. Law Rep. 613; Eckler v. Galbraith, 12 Bush (Ky) 71; Tolle v. Smith's Ex'r, 98 Ky. 464, 33 S. W. 410; Brashears v. Combs, 39 Am. B. A. 98, 174 Ky. 344, 192 S. W. 482. It is not clear, however, whether the cause of action is upon the old promise with the discharge in bankruptcy waived by the new promise, or is upon the new promise as a separate and new obligation supported by moral consideration, as an



exception to the general rule of consideration. The authorities throughout the country are in conflict on this issue with the weight in favor of the view that the action lies upon the new promise. See 3 R.C.L., Bankruptcy, Sec. 147; 8 Corpus Juris Secundum, Bankruptcy, Sec. 583, subdivision (d)."

In the first place this contention is not in accord with the facts in the case before us. The objecting creditor's claim is based upon a judgment obtained in an action for the recovery of money owing on certain notes scheduled in the previous bankruptcy. The bankrupt answered by admitting the obligation and setting up his discharge as a defense in bar. The creditor replied, by way of avoidance, that the bankrupt had waived his discharge by agreeing to pay the debt notwithstanding his bankruptcy. Remington on Bankruptcy, Fifth Edition, states: "The new promise need not be pleaded or proved in the first instance. To do so would be to anticipate a defense. The [15] bar of the discharge is merely matter of defense to be pleaded. If pleaded, then the new promise is in turn to be pleaded, by way of avoidance." Section 3512, p. 675; Gruenberg v. Trainor, 81 N. Y. Supp. 675, 11 A.B.R. 776. The reduction of the creditor's notes to judgment served merely to change the form of the debt but did not make a new or different one. In re Summer (C.C.A. 2d) 107 F. (2d) 396; 41 A.B.R. (N.S.) 246; In re Kuffler, 168 Fed. 1021; cert. den. 214 U. S. 520; In re Schnabel, 166 Fed. 383.

We are thus faced with the fact that the judgment from which the bankrupt seeks a discharge

in his second bankruptcy represents the same debt scheduled in his former bankruptcy. In *United States National Bank of La Grande v. Miller*, 118 Or. 280, 246 Pac. 726, it was held that an action to recover a debt discharged in bankruptcy may be based either on the original debt or on the new promise. In *Parker v. Smith*, 143 Wash. 677, 255 Pac. 1026, it was held that an oral promise to pay a promissory note discharged in bankruptcy revives the obligation as a whole and recovery may be had upon the original note, including the provision for an attorney's fee. To like effect are: *Pierce v. Fleming*, 205 Ia. 1281, 217 N.W. 860; *Stern v. Bradner Smith & Co.*, 225 Ill. 430, 80 N.E. 307, 116 Am. St. R. 151; *Badger v. Gilmore* 33 N.H. 361, 66 Am. D. 729; *McClintic-Marshall Co. v. City of New Bedford*, 239 Mass. 216, 131 N.E. 444; *DeWalt v. Heeren*, 197 N.W. 868, 50 N.D. 804; *Herrington v. Davitt*, 220 N.Y. 162, 115 N.E. 476, 1 A.L.R. 1700. In the latter case the court said: "The right of action is given by a new and efficacious promise. The practice of bringing the action upon the original demand is, however, sanctioned by usage. The discharge in bankruptcy is, under such practice, regarded as a discharge of the debt sub modo only, and the new promise as a waiver of the bar to the recovery of the debt created by the discharge. The new promise, with such other facts as are essential to constitute it a valid cause of action, may, however, be alleged." This case is significant in that New York is one of the few states [16] requiring a promise to pay

a discharged debt to be in writing. Notwithstanding this requirement the New York Court of Appeals, of which Mr. Justice Cardozo was then a member, held, "The action was properly brought upon the note. For the purpose of the remedy, the original debt might still be considered the cause of action."

Collier on Bankruptcy, 14th Edition, in dealing with the question of the revival of a discharged debt by a new promise, states: "The general rule is that a discharge affects only the remedy of the creditor and the obligation itself is not cancelled. It now remains to be seen whether the remedial bar of a discharge may be removed in any way. The Bankruptcy Act does not provide for the revival of debts discharged in bankruptcy. The law in the various states governs this matter, and it is generally agreed that the bar of a discharge may be waived by the making of a new promise. In reaching this decision, the courts have employed various theories; some courts have found consideration for the new promise in the form of a past legal obligation plus a present moral obligation, while other courts have declared that no new consideration is necessary to support the waiver." Par. 17.33, Page 1671.

In *Helms v. Holmes*, (C.C.A. 4th) 129 F. (2d) 263, 50 A.B.R. (N.S.) 133, 141 A.L.R. 1367, the court said: "It must be remembered that a discharge in bankruptcy is neither a payment nor an extinguishment of debts. It is simply a bar to their enforcement by legal proceedings. \* \* \*

Thus, the bankrupt is merely given a personal defense which is waived if he chooses not to avail himself of it. This rule that a failure so to plead operates in law as a waiver of the defense has been uniformly followed by state and federal courts alike."

In a case decided recently in the Seventh Circuit, the foregoing case was cited with approval. The court then said: "A discharge is neither a payment nor an extinguishment of a debt. [17] When properly pleaded, it is a bar to the enforcement of an existing debt by legal proceedings and, thus, it amounts merely to a personal defense which is waived if the debtor chooses not to avail himself of it. A discharged debt may be renewed by a new promise and, even though a state court is advised of a discharge, in the absence of a plea setting up the defense, it has a right to assume either that the bankrupt has renewed his debt by a new promise or that, by his silence, he tacitly exhibits an intent to waive the defense. We know of no basis upon which a court of equity can relieve a defendant from liability because of this failure to plead a personal defense where no ground for the intervention of equity is presented." In *re Innis*, (C.C.A. 7th) 140 F. (2d) 479, 55 A.B.R. (N.S.) 427; cert. den. 64 S. Ct. 1048.

With due deference to the authorities cited by bankrupt's counsel to support his contention that the promise to pay a discharged debt creates an altogether new obligation, separate and distinct from the discharged debt, it is respectfully sug-

gested that perhaps the reasoning of these decisions are based upon a misconception of the function of the new promise necessary to revive a discharged debt. It is true that the decisions universally hold that such a promise must be express, clear and unequivocal. A mere acknowledgment of the debt, or an expression of hope, desire, expectation or intention to pay is insufficient. It must be an express promise to pay a specific debt. A few states, not including Oregon, require the promise to be in writing. However, as we have seen, a discharge in bankruptcy does not extinguish the debt. It merely affords a personal defense in bar which may be waived either by a new promise or a failure to plead it in an action brought upon a discharged debt. Thus the only function of the new promise is to serve as an express waiver of the defense. As most authorities state, it merely revives or renews the legal obligation. It restores the remedy taken away by the discharge. It is the test applied by the court in determining whether the [18] discharge has been waived. No consideration is necessary. In the authorities cited by counsel the courts invoke a moral obligation as the consideration to support the new debt which they seek to create out of the promise to pay the discharged obligation. In this connection Williston states: "The law in most of the United States, as in England, has rejected the principle of moral consideration, even though some exceptional cases of liability on promises made without present consideration may still exist as in the case of promises to pay debts barred



by the Statute of Limitations, or by a discharge in bankruptcy. Such cases are now rested on other grounds and moral consideration as such is held insufficient to support a promise. There can be no question that in most states a plaintiff would invite disaster if he endeavored to support an action on a promise on the theory that the promise was supported by moral consideration without more." Williston on Contracts, Revised Edition, Section 148, Page 522.

The reasoning adopted herein is the same as that pursued by Judge Harrington in *Tubbs v. McCabe* in the Superior Court of Delaware, 165 Atl. 336. There, action was brought upon a judgment on a note which had been scheduled in a bankruptcy of the judgment debtor in Virginia. The only issue is stated as follows: "The defendant does not deny that he expressly promised to pay the plaintiffs' debt but claims that the action must be on the new promise on which their rights are based. He further claims that as such promise was made in the State of Virginia, by the express provisions of a statute of that state such promise, to be effective, must be in writing." The court held that the action was brought properly on the old judgment. The following are pertinent excerpts from the opinion, omitting citations:

"The effect of a discharge in bankruptcy may, therefore, not only be waived by a failure to plead and prove such discharge but it may also be waived by a clear and specific promise to pay made by the bankrupt at any time after his petition is filed. [19]



“In this country it is clear, however, that no new consideration is necessary to support the promise of a bankrupt to pay a debt the mere collection of which has been barred by the Bankruptcy Act.

\* \* \* \* \*

“True, the new promise may, as a general rule, even be conditional and such a promise, if made, is the measure of the plaintiffs’ right whether relied on to raise the bar of the statute of limitations, or in a case where a defendant has been adjudicated a bankrupt (1 Willist. on Contr. Sections 196, 203; 7 Rem. on Bankr. Section 3506); but where the statute of limitations is involved it is well settled in this state that the action should be on the old debt and not on the new promise to pay.

“This can only be on the ground that the defense of the statute is waived and the same general principles naturally apply to promises to pay made by a bankrupt. Restatement of the Law on Contr., vol. 1, Sec. 86; 7 Rem. on Bankr. Sec. 3499.

“In fact, the old theory that the rights of the plaintiffs in such cases are based on a moral consideration has now been very generally exploded. 1 Willist. on Contr. Sec. 148.

“It is true that for some reason a specific promise to pay is necessary to remove the bar of the statute in bankruptcy cases while a promise to pay will be inferred from a mere acknowledgement of a subsisting demand where the statute of limitations is involved, but whatever the reason for this differ-

ence may be, it does not affect the rule above stated."

From the facts and the law as we see it, our conclusions are: 1. The debt owing the objecting creditor is the same obligation from which the bankrupt received a discharge in his first bankruptcy. 2. Having waived his discharge as to this debt, he cannot seek a second discharge from the same obligation. To permit him to do so, would be an abuse of process and an imposition upon the court. A qualified discharge is being entered today in which the objecting creditor's debt is excluded on the ground that the bankrupt had been relieved of the obligation under the Bankruptcy Act and had waived his right thereto.

Filed at Portland, Oregon, this 3rd day of March, 1945.

S/ ESTES SNEDECOR,  
Referee in Bankruptcy.

[Endorsed]: Filed March 3, 1945. Estes Snedecor, Referee in Bankruptcy.

[Endorsed]: Filed March 7, 1945. Lowell Mundorff, Clerk. [20]

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[Title of District Court and Cause.]

### DISCHARGE OF BANKRUPT

At a session of the court of Bankruptcy held in and for the District of Oregon before Estes Snede-

cor, Referee in Bankruptcy, at Portland, Oregon, this 3rd day of March, 1945;

It appearing that Bernard G. Shepherd of Portland, in the County of Multnomah, State of Oregon, was duly adjudged a bankrupt on a petition filed by him on the 16th day of December, 1941; and

It further appearing that, after due notice by mail, objections to the discharge of the said bankrupt were filed and, after due notice by mail, were heard and the first and second specifications were not sustained; the third specification is sustained on the ground that the bankrupt had previously received a discharge from the obligation owing to the objecting creditor and had waived his right thereto under the Bankruptcy Act and cannot seek a second discharge from the same obligation:

Therefore, It Is Ordered that the said Bernard G. Shepherd be, and he hereby is, discharged from all debts and claims which are made provable by said Act against his estate, except such debts as are, by said Act, excepted from the operation of a discharge in bankruptcy, and except the judgment owing to Mildred McDonald on which the bankrupt had waived a discharge obtained in a former bankruptcy.

/s/ ESTES SNEDECOR,

Referee in Bankruptcy.

[Endorsed]: Filed March 3, 1945. Estes Snedecor, Referee in Bankruptcy.

[Endorsed]: Filed March 3, 1945. Lowell Munderff, Clerk. [21]

[Title of District Court and Cause.]

PETITION FOR REVIEW OF REFEREE'S  
ORDER BY JUDGE

To Estes Snedecor, Esq., Referee in Bankruptcy:  
The Petition of Bernard G. Shepherd respectfully  
represents:

1. That your Petitioner is the Bankrupt herein.
2. That, heretofore, this honorable court made an order in the above entitled bankruptcy proceedings fixing the 4th day of May, 1942, as the last day within which specifications of objection to the bankrupt's discharge herein might be filed.
3. That one Mildred Muck, a creditor duly scheduled by the Bankrupt in the above entitled bankruptcy proceedings, did, on the 4th day of May, 1942, file three specifications of objection to the Bankrupt's discharge.

That thereafter the said specifications of objection came on regularly for hearing on the 7th day of August, 1944, and thereupon, and on said date, an order was entered overruling and denying the first and second specification of objection, and the Referee took under advisement the said third specification of objection. That on the third day of March, 1945, an order was duly made and entered herein sustaining the third specification of objection to the Bankrupt's discharge, and giving and granting the Bankrupt a qualified discharge which excepted and excluded from its provisions the operation thereof on the indebtedness of Mildred Muck, said

order being in words and figures, as follows; to-wit:

At a session of the court of Bankruptcy held in and for the District of Oregon before Estes Snedecor, Referee in Bankruptcy, at Portland, Oregon, this 3rd day of March, 1945; [22]

It appearing that Bernard G. Shepherd of Portland, in the County of Multnomah, State of Oregon, was duly adjudged a bankrupt on a petition filed by him on the 16th day of December, 1941; and

It further appearing that, after due notice by mail, objections to the discharge of the said bankrupt were filed and, after due notice by mail, were heard and the first and second specifications were not sustained; the third specification is sustained on the ground that the bankrupt had previously received a discharge from the obligation owing to the objecting creditor and had waived his right thereto under the Bankruptcy Act and cannot seek a second discharge from the same obligation:

Therefore, It Is Ordered that the said Bernard G. Shepherd be, and he hereby is, discharged from all debts and claims which are made provable by said Act against his estate, except such debts as are, by said Act, excepted from the operation of a discharge in bankruptcy, and except the judgment owing to Mildred McDonald on which the bankrupt had waived a discharge obtained in a former bankruptcy.

That the said order is erroneous for the following reasons:



1. That the Referee erred in finding and holding that the debt owing by the Bankrupt to Mildred Much, being a judgment entered against the Bankrupt on the 7th day of August, 1935, and scheduled by the Bankrupt in his voluntary petition in bankruptcy herein, is the same debt as the debt owing to Mildred McDonald, now Mildred Muck, by the Bankrupt herein and scheduled by him in his petition in bankruptcy filed June 27, 1931.

2. That the Referee erred in finding and holding that because the Bankrupt herein by making a new promise to Mildred McDonald, now Mildred Muck, to pay her the indebtedness from which he was discharged in his bankruptcy proceedings initiated June 27, 1931, followed by a judgment in favor of Mildred Muck entered the 7th day of August, 1935, waived his right to a discharge from said judgment in the present bankruptcy proceedings.

3. That the referee erred in finding and holding that the Bankrupt herein was not entitled to a discharge from the indebtedness owing the said Mildred Muck, and duly scheduled in this bankruptcy proceedings, for the reason that the Bankruptcy Act of the United States, which was in full force and effect at the time of the adjudication [23] in these proceedings, expressly provides that the Bankrupt is entitled to a discharge from all of his provable debts, unless he has committed one of the acts expressly set forth in Section 14 of said Bankruptcy Act, it not being claimed in the specifications of objection filed by the said Mildred Muck that any of



such prohibitive acts had been committed by said bankrupt.

4. That the Referee erred in finding and holding that the Bankrupt was not entitled to a discharge from the indebtedness due Mildred Muck duly scheduled in these proceedings and duly proved by the said Mildred Muck.

5. That the Referee erred in finding and holding that the Bankrupt waived his discharge on the indebtedness of Mildred Muck, duly scheduled in these bankruptcy proceedings, for the reason that there is no evidence in the record produced before the Referee by said objecting creditor, which proves, or tends to prove, or show, that the Bankrupt waived his discharge in this proceeding on the indebtedness of Mildred Muck.

6. That the Referee erred in failing to sustain the Bankrupt's motion to strike the third specifications of objection filed by Mildred Muck in these proceedings.

7. That the Referee erred in finding and holding that the Bankrupt herein was not entitled and could not seek a second discharge from the same obligation owing Mildred McDonald, now Mildred Muck, as that scheduled in his first bankruptcy proceeding filed June 27, 1931.

8. That the Referee erred in finding and holding that to allow a discharge in these proceedings from the indebtedness owing Mildred Muck would be an abuse of process and an imposition on this court, for the reason that the Bankrupt is entitled, as a matter of right under the Bankruptcy Act of

the United States to a discharge from said indebtedness.

9. That the Referee erred in entering a qualified and [24] restricted order of discharge, instead of granting a complete and full discharge to the Bankrupt herein from all of his provable debts, as provided by the Bankruptcy Act of the United States.

10. That the Referee erred in finding and holding that the Bankrupt waived all rights under the Bankruptcy Act of the United States at any time whatsoever, so far as the indebtedness of Mildred Muck is concerned, by making a promise to pay the indebtedness of Mildred Muck after the same had been discharged in his first bankruptcy proceedings of June 27, 1931.

11. That the Referee erred in finding and holding that the Bankrupt, in this proceeding initiated more than six years after his discharge in the bankruptcy proceedings initiated June 27, 1931, had no legal right to schedule an indebtedness due and owing Mildred Muck, and thereby obtained a discharge in this bankruptcy proceedings from said indebtedness.

12. That the Referee erred in finding and holding that the new promise made by the Bankrupt to pay the indebtedness of Mildred Muck theretofore discharged in his bankruptcy proceedings in June 27, 1931, made said indebtedness and any further judgment thereafter rendered thereon a nondischargeable debt in any future, valid bank-

ruptcy proceedings initiated by or against the Bankrupt.

Wherefore, your petitioner prays for a review of said order by the Judge, and that said order be vacated and set aside and that a new order be entered herein giving and granting the Bankrupt herein a full and complete discharge from all of his provable debts scheduled in this proceedings, including the indebtedness owing the objecting creditor, Mildred Muck.

Dated this 7th day of March, 1945.

BERNARD G. SHEPHERD,  
Petitioner.

COAN & ROSENBERG,  
Attorneys for Petitioner. [25]

United States of America,  
County of Multnomah,  
State of Oregon—ss.

I, Bernard G. Shepherd, being first duly sworn, on oath say that I am the Petitioner herein; that I have read the foregoing petition and the facts therein set forth are true.

BERNARD G. SHEPHERD.

Subscribed and sworn to before me this 7th day of March, 1945.

[Seal] RALPH A. COAN,  
Notary Public for Oregon.

My commission expires May 19, 1948.

Due and legal service of the foregoing, by receipt of a duly certified copy thereof, as required by law,

is hereby accepted in Multnomah County, Oregon,  
on this 7 day of March, 1945.

W. E. RICHARDSON,  
Attorney for Objecting  
Creditor.

[Endorsed]: Filed March 7, 1945. Estes Snedecor, Referee in Bankruptcy.

[Endorsed]: Filed March 7, 1945. Lowell Mundorff, Clerk. [26]

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[Title of District Court and Cause.]

#### MEMO OF DECISION

The Referee's order is affirmed, and I adopt the Referee's opinion as the opinion of the court on the law of the case.

Dated at Portland, Oregon, this 31st day of July, 1945.

CLAUDE McCOLLOCH,  
Judge.

[Endorsed]: Filed July 31, 1945, Lowell Mundorff, Clerk. [27]

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[Title of District Court and Cause.]

#### ORDER

This cause was heard by the court on the petition of the bankrupt to review an order of the referee qualifying the discharge of the bankrupt, the bank-

rupt appearing by Mr. Quincy L. Matthews and by Mr. Ralph A. Coan, of counsel, and the objecting creditor appearing by Mr. W. E. Richardson, of counsel; and the court having heard the argument of counsel and being fully advised in the premises,

It Is Ordered that the opinion of the referee in this cause be and the same is hereby adopted as the opinion of this court, and it is

Further Ordered That the Order of the referee discharging the bankrupt with qualifications, filed in the office of the Clerk on March 3, 1945, be and the same is hereby in all respects affirmed.

CLAUDE McCOLLOCH,  
Judge.

[Endorsed]: Filed August 1, 1945. Lowell Mundorff, Clerk. [28]

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[Title of District Court and Cause.]

### NOTICE OF APPEAL

Notice is hereby given that Bernard G. Shepherd, bankrupt herein, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from an Order dated August 1, 1945, affirming the Order of the Referee in Bankruptcy discharging the bankrupt with qualifications, which last mentioned or-

der was filed in the office of the Clerk on the third day of March, 1945.

RALPH A. COAN,

Attorney for Bernard G.  
Shepherd, Bankrupt-  
Appellant.

[Endorsed]: Filed August 20, 1945. Lowell  
Mundorff, Clerk. [29]

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[Title of District Court and Cause.]

### BOND ON APPEAL

Know All Men by These Presents, that we, Bernard G. Shepherd, as principal and National Surety Corporation, incorporated under the laws of the State of New York, as surety, are held and firmly bound unto Mildred Muck in the sum of \$250.00 for the payment of which well and truly to be made we bind ourselves, our administrators, successors and assigns, jointly and severally firmly by these presents.

Sealed with our seals and dated this 20th day of August, 1945.

Whereas, an order was entered herein on the first day of August, 1945, in the above entitled bankruptcy proceedings wherein Bernard G. Shepherd was bankrupt and Mildred Muck was objecting creditor, which said order affirmed an order made by Estes Snedecor, Referee, discharging the bankrupt



with qualifications, and the said Bernard G. Shepherd did on the 20th day of August, 1945, file Notice of Appeal from said order as required by law, and

Whereas, a bond for costs on appeal in the sum of \$250, is required by law to be filed with the said notice.

Now, therefore, the condition of this obligation is such that if the said Bernard G. Shepherd shall pay all costs which may be awarded if the said appeal is dismissed or the said order affirmed, and such costs as the Appellate Court may award if the said order is modified. [30] then this obligation shall be void, otherwise the same shall be and remain in full force and virtue.

BERNARD G. SHEPHERD,  
Principal.

NATIONAL SURETY  
CORPORATION.

By W. B. GILHAM,  
Attorney-in-Fact.

Countersigned:

By W. B. GILHAM,  
Resident Agent.

[Endorsed]: Filed August 20, 1945, Lowell Munderff, Clerk. [31]

[Title of District Court and Cause.]

DESIGNATION OF THE PORTIONS OF THE  
RECORD AND PROCEEDINGS TO BE  
CONTAINED IN THE RECORD ON AP-  
PEAL.

Bernard G. Shepherd, Appellant, hereby designates the following portions of the record to be contained in the record on appeal herein to the Circuit Court of Appeals for the Ninth Circuit.

1. Certificate of Referee on Petition of Bankrupt for Review of Referee's Order Qualifying Bankrupt's Discharge.

2. Specifications of Objections to Discharge and Petition for Refusal.

3. Order Denying First and Second Specifications of Objection to Bankrupt's Discharge.

4. Motion to Strike Third Specification of Objection and Order Denying Motion.

5. Referee's Opinion.

6. Referee's Order Discharging Bankrupt with Qualifications.

7. Petition for Review of Referee's Order.

8. Memo Decision of District Judge.

9. Order of District Court Affirming Referee's Order Discharging Bankrupt with Qualifications.

10. Notice of Appeal.

11. Bond on Appeal.

12. The following exhibits: Objector's Exhibits 1 and 2 and Bankrupt's Exhibits 6 and 7.

13. This designation of Portions of Record.

RALPH A. COAN,

Attorney for Bernard G. Shepherd, Bankrupt-Appellant.

[Endorsed]: Filed August 22, 1945. Lowell Mundorff, Clerk. [32]

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[Title of District Court and Cause.]

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY ON APPEAL.

Bernard G. Shepherd, who has filed a Notice of Appeal in this Court to the Circuit Court of Appeals for the Ninth Circuit from an Order made and entered on the first day of August, 1945, affirming an Order of the Referee in Bankruptcy discharging the Bankrupt with qualifications, will rely on the following points on said appeal.

That said Order is erroneous and should be reversed for the following reasons:

1. That the District Court erred in finding and holding that the debt owing by the Bankrupt to Mildred Muck, being a judgment entered against the Bankrupt on the 7th day of August, 1935, and scheduled by the Bankrupt in his voluntary petition herein, is the same debt as a debt owing to Mildred McDonald, now Mildred Muck, and scheduled

in the Bankrupt's petition and bankruptcy filed June 27, 1931.

2. That the District Court erred in finding and holding that the Bankrupt waived his right to a discharge in the present bankruptcy proceedings from a judgment obtained by Mildred Muck on the 7th day of August, 1935, based upon a new promise to pay the indebtedness from which Bernard G. Shepherd was discharged in his bankruptcy proceedings filed June 27, 1931.

3. That the District Court erred in finding and holding that Bernard G. Shepherd, Bankrupt herein, was not entitled to a discharge from the indebtedness owing Mildred Muck which was duly [33] scheduled in these proceedings for the reason that the Bankruptcy Act of the United States expressly provides that a bankrupt is entitled to a discharge from all his provable debts unless he has committed one or more of the acts enumerated in Section 14 (c) of the Bankruptcy Act.

4. That the District Court erred in finding and holding that the Bankrupt was not entitled to a discharge from the indebtedness owing Mildred Muck duly scheduled, proved and allowed in these proceedings.

5. That the District Court erred in refusing to sustain Bankrupt's motion to strike the third specification of the objection filed by Mildred Muck, objecting creditor, in opposition to Bankrupt's discharge.

6. That the District Court erred in finding and holding that Bernard G. Shepherd, Bankrupt, was

not entitled to and could not seek a second discharge from the same obligation owing Mildred McDonald, now Mildred Muck, as that scheduled in his first bankruptcy proceeding filed June 27, 1931.

7. That the District Court erred in finding and holding that to grant a discharge in this proceeding from the indebtedness owing Mildred Muck would be an abuse of processes and an imposition on the Court for the reason that a Bankrupt is entitled as a matter of right under the Bankruptcy Act to a discharge from all provable debts unless he has committed one of the acts set forth in Section 14 (c) of said Act.

8. That the District Court erred in entering a qualified and restricted order of the discharge instead of granting Bankrupt a complete and full discharge from all his provable debts.

9. That the District Court erred in finding and holding that Bankrupt waived all rights under the Bankruptcy Act to at any time whatsoever obtain a discharge upon the indebtedness of Mildred Muck by making a promise to pay said indebtedness subsequent to [34] the discharge entered in Bankrupt's first bankruptcy proceedings.

10. That the District Court erred in finding and holding that the Bankrupt had no right to schedule in this proceeding an indebtedness due and owing Mildred Muck because said indebtedness was discharged in his former bankruptcy proceeding.

11. That the District Court erred in finding and holding that the new promise made by Bankrupt to pay the indebtedness of Mildred Muck thereto-



fore discharged in his bankruptcy proceedings of June 27, 1931, made said indebtedness and any judgment obtained thereon a non-dischargeable debt in any valid bankruptcy proceedings filed by or against the Bankrupt at any time thereafter.

12. That the District Court erred in entering an order adopting the opinion of the Referee as the opinion of the District Court and in affirming the order of the Referee discharging the Bankrupt with qualifications.

RALPH A. COAN,

Attorney for Bernard G.

Shepherd, Appellant [35]

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[Title of District Court and Cause.]

### AFFIDAVIT OF SERVICE

State of Oregon, County of Multnomah—ss.

I, Ralph A. Coan, being duly sworn, deposes and say that I did on the 22d day of August, 1945, at the hour of 11:00 A. M., of said day, mail to W. E. Richardson, attorney for Mildred Muck, objecting creditor, addressed to his office, Alisky Building, Portland, Oregon, that being his last known address, a full true and correct copy of Bernard G. Shepherd, Appellant's "Designation of the Portion of the Record and Proceedings to be Contained in the Record on Appeal" and also "Statement of Points on which Appellant Intends to Rely on Appeal," certified to by me as being full, true and correct copies of the originals, as provided by Rule 5 (b) of the Rules of



Civil Procedure of the District Court of the United States.

RALPH A. COAN

Subscribed and sworn to before me this 22d day of August, 1945.

(Seal)

BURTON L. COAN,

Notary Public for Oregon.

My commission expires August 26, 1946. [36]

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OBJECTOR'S EXHIBIT No. 1

Book 568, page 52.

No. 114-088

In the Circuit Court of the State of Oregon  
for the County of Multnomah

MILDRED McDONALD,

Plaintiff

vs.

B. G. SHEPHERD and LORENZO MANSFIELD,  
Defendant.

JUDGMENT

Be it remembered that this cause came on for hearing on the 6th day of February, 1935, before Honorable Robert Tucker, one of the judges of the above entitled Court. The plaintiff appearing in person and by her attorneys, Frank E. Manning and Robert G. Smith, the defendant B. G. Shepherd appearing in person and by Paul M. Long and Christopherson & Matthews, and the defendant Lorenzo Mansfield not having been served with process appearing neither in person nor by counsel.

Twelve persons legally qualified were examined and sworn to try the case. After the opening statements of attorneys, the introduction of testimony, the closing arguments and the instructions of the court, the jury retired to consider of its verdict. After being out for a time the jury returned into court and presented its verdict as follows:

“We the jury in the above entitled cause find for the plaintiff and against the defendant B. G. Shepherd in the sum of \$2543.95 with interest thereon from June 10, 1930, at the rate of six per cent per annum.

OTTO EKLUND,

Foreman of the Jury.”

“Dated Feb. 6, 1935.

Said verdict was duly received and filed and the jury discharged from further consideration of this cause.

Pursuant to said verdict and the law, it is now and hereby ordered and adjudged that Mildred McDonald do have and recover of and from B. G. Shepherd the sum of \$2543.95 with interest thereon at the rate of 6% per annum, together with her costs and disbursements therein, amounting to the sum of \$. . . . to be taxed.

ROBERT TUCKER,

Judge.

Dated February 7th, 1935.

Judgment docketed Feb. 7, 1935, Book 31, page 207. [37]

No. 26745

State of Oregon, County of Multnomah—ss.

I, A. A. Bailey, County Clerk and Ex Officio Clerk of the Circuit Court of the State of Oregon for the County of Multnomah, a Court of Record, do hereby certify that the foregoing copy of Judgment (Mildred McDonald, Plaintiff, vs. B. G. Shepherd and Lorenzo Mansfield, Defendants) No. 114-088, has been compared by me with the original and that it is a correct transcript therefrom, and of the whole of such original Judgment, as the same appears of record in my office and in my custody.

In Testimony Whereof, I have hereunto set my hand and affixed the seal of said court, this 7th day of January, A. D. 1942.

(Seal)

A. A. BAILEY,  
County Clerk.

By MARY DUNKIN,  
Deputy. [38]

\$148.50

Sept. 25, 1929

60 days after date, without grace, we promise to pay to the order of M. McDonald at Portland, Ore., One Hundred Forty-eight and 50/100 Dollars, in Gold Coin of the United States of America, of the present standard value, with interest thereon in like Gold Coin, at the rate of            per cent. per from            until paid, for value received. Interest to be paid Without Int. and if not so paid, the whole sum of both principal and interest to become immediately due and collectible, at the option of the holder of this note. And in case suit or action is institut-

ed to collect this note, or any portion thereof, promise and agree to pay, in addition to the costs and disbursements provided by statute, such additional sum, in like Gold Coin, as the Court may adjudge reasonable, for attorney's fees to be allowed in said suit or action.

LORENZO MANSFIELD

STUDIOS

B. G. SHEPHERD,

Secty & Tr.

\$192.50

Sept. 25, 1929

60 days after date, without grace, we promise to pay to the order of M. McDonald—at Portland, Oregon, One Hundred Ninety-two and 50/100 Dollars, in Gold Coin of the United States of America, of the present standard value, with interest thereon in like Gold Coin, at the rate of            per cent. per from            until paid, for value received. Interest to be paid Without Interest and if not so paid, the whole sum of both principal and interest to become immediately due and collectible, at the option of the holder of this note. And in case suit or action is instituted to collect this note, or any portion thereof,            promise and agree to pay, in addition to the costs and disbursements provided by statute, such additional sum, in like Gold Coin, as the Court

may adjudge reasonable, for attorney's fees to be allowed in said suit or action.

No.

LORENZO MANSFIELD  
STUDIS  
B. G. SHEPHERD,  
Secty.

\$187.00

October 9, 1929

90 days after date, without grace, we promise to pay to the order of M. McDonald at Portland, Oregon,                   Dollars, in Gold Coin of the United States of America, of the present standard value, with interest thereon in like Gold Coin, at the rate of           per cent. per           from           until paid, for value received. Interest to be paid Without Interest and if not so paid, the whole sum of both principal and interest to become immediately due and collectible, at the option of the holder of this note and in case suit or action is instituted to collect this note or any portion thereof, promise and agree to pay, in addition to the costs and disbursements provided by statute, such additional sum, in like Gold Coin, as the Court may adjudge reasonable, for attorney's fees to be allowed in said suit or action.

No.

LORENZO MANSFIELD  
STUDIOS  
B. G. SHEPHERD

\$550.00

Oct. 17, 1929

60 days after date, without grace, we promise to pay to the order of M. McDonald—at Portland, Oregon, Five Hundred Fifty Dollars, in Gold Coin of the United States of America, of the present standard value, with interest thereon in like Gold Coin, at the rate of        per cent. per        from until paid, for value received. Interest to be paid No int. and if not so paid, the whole sum of both principal and interest to become immediately due and collectible, at the option of the holder of this note. And in case suit or action is instituted to collect this note, or any portion thereof,        promise and agree to pay, in addition to the costs and disbursements provided by statute, such additional sum, in like Gold Coin, as the Court may adjudge reasonable, for attorney's fees to be allowed in said suit or action.

No.

LORENZO MANSFIELD  
STUDIOS

B. G. SHEPHERD,  
Secty.

\$400.00

Feb. 5, 1930

90 days after date, without grace, we promise to pay to the order of M. McDonald at Portland, Oregon, Four Hundred Dollars, in Gold Coin of the United States of America, of the present standard value, with interest thereon in like Gold Coin, at the rate of 7 per cent. per annum from date until paid, for value received. Interest to be paid.



and if not so paid, the whole sum of both principal and interest to become immediately due and collectible, at the option of the holder of this note. And in case suit or action is instituted to collect this note, or any portion thereof,                      promise and agree to pay, in addition to the costs and disbursements provided by statute, such additional sum, in like Gold Coin, as the Court may adjudge reasonable, for attorney's fees to be allowed in said suit or action.

No.

B. G. SHEPHERD

LORENZO MANSFIELD

Be It Remembered, that at a regular term of the Circuit Court of the State of Oregon for the County of Multnomah, begun and held at the County Court House in the City of Portland, in said County and State, on Monday, the 4th day of February, A .D. 1935, the same being the First Monday, in said month, at the time fixed by law for holding a regular term of said Court.

Present, Hons. Jacob Kanzler, James W. Crawford, Robert Tucker, Hall S. Lusk, Louis P. Hewitt, James P. Stapleton, George Tazwell, John P. Winter, and Clarence H. Gilbert, Judges.

Whereupon, on this Thursday, the 7th day of February, A. D. 1935, the same being the 4th judicial day of said term of Court, among other proceedings, the following was had, towit:

## Proof of Claim By Individual

Form No. 28.

In the District Court of the United States  
for the District of Oregon

In Bankruptcy—No. B-26580

In the Matter of

BERNARD G. SHEPHERD

State of Oregon, County of Multnomah—ss.

I, Mildred Muck, formerly Mildred McDonald of No. 6330 S. E. 36th Street, in Portland, County of Multnomah, State of Oregon, being duly sworn, deposes and says:

1. That Bernard G. Shepherd, the above named bankrupt, was at and before the filing by (or against) him/it of the petition for adjudication of bankruptcy, and still is, justly and truly indebted (or liable) to said deponent in the sum of \$2543.95.

2. That the consideration of said debt (or liability) is as follows: Money loaned to the bankrupt which claim has been reduced to judgment, with interest thereon from June 10, 1930, at 6% per annum plus \$32.25 cost as shown by cost bill on file in said Court with interest thereon at the rate of 6% per annum from February 7, 1935.

3. That no part of said debt (or liability) has been paid, except

4. That there are no set-offs or counterclaims to said debt (or liability except

5. That deponent does not hold, and has not, nor has any person by his order, or to his knowledge or

belief, for his use, had or received any security or securities for said debt (or liability), except

6. (If the debt or liability is founded upon an instrument of writing:) That the instrument upon which said debt (or liability) is founded is attached hereto (or is lost or destroyed, as set forth in the affidavit attached hereto).

7. (If the debt is founded upon an open account): That the said debt was (or will become) due on February 7, 1935 (or that the average due date thereof is ): that no date or other negotiable instrument has been received for such [39] account or any part thereof (or that the said debt is evidenced by a note (or other negotiable instrument), which is attached hereto); and that no judgment has been rendered thereon, except that said claim was reduced to judgment in the Circuit Court, Multnomah County, Oregon, on the 7th day of January, 1935, Clerk's No. 114-088, a cerified copy of which said judgment is hereto attached and made a part hereof.

**MILDRED MUCK**

**Creditor**

Subscribed and sworn to before me this 12th day of Jan., 1942

(Seal)

**NELSON A. FROST,**

**Notary Public for Oregon**

My Commission expires June 9, 1945

## POWER OF ATTORNEY

Form No. 18

To Frank E. Manning and Mildred Muck:

I, Mildred Muck, of Portland, in the County of Multnomah, State of Oregon, do hereby authorize you, or any of you, with full power of substitution, to attend all meetings of creditors of the bankrupt aforesaid, and all adjournments thereof, at the places and times appointed by the Court, and for me and in my name to vote for or against any proposal or resolution that may be then submitted under the Act of Congress relating to bankruptcy, to vote for a trustee or trustees of the estate of the said bankrupt and for a committee of creditors, to accept any arrangement or wage-earner's plan, proposed by said bankrupt in satisfaction of his debts, and to receive payment of dividends, and payment or delivery of money or of other consideration due me under such arrangement or wage-earner's plan, and for any other purpose in my interest whatsoever; and with like powers to attend and vote at any other meeting or meetings of creditors, or sitting or sittings of the court, which may be held therein for any of the purposes aforesaid.

In witness whereof I have hereunto signed my name and affixed my seal the 6th day of January, 1942.

(Seal)

MILDRED MUCK

Formerly Mildred McDonald,  
Claimant.

Signed, sealed and delivered in the presence of

-----

Acknowledged before me this 6th day of Jan.,  
1942.

(Seal)

NELSON A. FROST

Notary Public for Oregon

My Commission expires June 9, 1945

[Endorsed]: Claim of Mildred Muck, Formerly  
Mildred McDonald. Amount \$2543.95, plus \$32.25  
and interest. [40]

[Endorsed]: Filed Jan. 12, 1942, Estes Snedocar,  
Referee in Bankruptcy.

[Endorsed]: Filed March 7, 1945, Cowell Mun-  
dorff, Clerk.

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## OBJECTOR'S EXHIBIT 2

Cloyd Rauch

Report

Case No. B-27580

## AGREEMENT

This Agreement made and entered into this 10th  
day of June 1929. By and between Lorenzo Mans-  
field and B. G. Shepherd hereinafter called party of  
the first part. And Mildred McDonald hereinafter  
called party of the Second part. Witnesseth:

That whereas the First party has taken over the  
Van Wie Mansfield Studios, Inc; and are now oper-  
ating and doing business under the firm name of Lo-  
renz Mansfield Studios, with the intention of chang-  
ing the name of the Van Wie Mansfield Studios, Inc;



to that of Lorenz Mansfield Studios, Inc; at an early date and within six months from date hereof.

And Whereas the second party has been interested in the financing of said Lorenz Mansfield Studios as an investment.

It Is Hereby Agreed As Follows: That for and in consideration of mutual promises one to the other and for and in consideration of Fourteen Hundred Dollars (\$1400.00) cash in hand paid by the second party, receipt of which is hereby acknowledged by the first party. The first party hereby agrees to sell a one third interest in the aforementioned Lorenz Mansfield Studios and upon the completion of the change in the name of said company to that of Lorenz Mansfield Studios, Inc; will forthwith issue certificates of stock in said corporation to the second party for one third of the capital stock of said corporation.

In addition to a one third interest in said corporation the second party is to receive the sum of \$14.00) Fourteen dollars per month, payable monthly, as interest and bonus for the use and investment of said principal sum of \$1400.00 aforementioned.

It Is Further Agreed that the second party will further finance the Lorenz Mansfield Studios by maintaining a separate fund in the approximate sum of Eleven Hundred Dollars (\$1100.00) and from time to time advancing to the first party, from said fund, various sums, at her option, to cover cost of materials required to complete the jobs or work which may be under contract or is being completed by said Lorenz Mansfield Studios, Inc.



And for all said moneys so advanced from time to time as aforesaid the first party will execute a promissory note in favor of the second party in the same amount together with interest and bonus equal to 10% and shall secure said note with an assignment of all right title and interest in and to the identical account for which said money is advanced each time. It being understood and agreed that [41] each of said notes with assignment shall be paid and taken up by the first party as soon as they have received payment from the respective customer on each identical job or contract.

It being the mutual agreement and understanding of the parties hereto that in the event of dissolution of the Lorenz Mansfield Studios at anytime prior to the completion of said change in name of said corporation or the issuing of said stock to the second party hereto, then, and in that event, the first party will assign to the second party enough good accounts to make full reimbursement to her for the \$1400.00 originally advanced to the first party aforementioned.

This agreement signed in triplicate this 27th day of August 1929. A. D.

(Seal)                      LORENZO MANSFIELD

(Seal)                      B. G. SHEPHERD

Party of the First part.

(Seal)                      MILDRED McDONALD

Party of the Second part.

[Endorsed]: Filed March 7, 1945. Lowell Mundorff, Clerk. [42]

## BANKRUPT'S EXHIBIT 6

Cloyd Rauch, Reporter. Case No. B27580

District Court of the United States

District of Oregon

No. B 16240 In Bankruptcy

In the Matter of

BERNARD G. SHEPHERD,

Bankrupt.

## DISCHARGE OF BANKRUPT

Whereas, Bernard G. Shepherd of Portland in the county of Multnomah in said District, has been duly adjudged a bankrupt, under the Acts of Congress relating to bankruptcy, and appears to have conformed to all the requirements of law in that behalf.

It Is Therefore Ordered by the Court that said Bernard G. Shepherd be discharged from all debts and claims which are made provable by said Acts against his estate, and which existed on the 26th day of June, A. D. 1931, on which day the petition for adjudication was filed by him; excepting such debts as are by law excepted from the operation of a discharge in bankruptcy.

Witness the Honorable John H. McNary, Judge of said District Court, and the seal thereof, this 21st day of October, A. D. 1931.

(Seal)

G. E. MARSH,

Clerk.

By L. S. ROGERS,

Deputy Clerk.

United States of America, District of Oregon—ss.

I, G. H. Marsh, Clerk of the United States District Court for the District of Oregon, do hereby certify that the foregoing copy of Discharge of Bankrupt, in cause No. B-16240, in the matter of Bernard G. Shepherd, bankrupt has been by me compared with the original thereof, and that it is a correct transcript therefrom, and of the whole of such original, as the same appears of record and on file at my office and in my custody.

In testimony whereof I have hereunto set my hand and affixed the seal of said court at Portland, in said District, this 29th of January, 1935.

(Seal) G. H. MARSH,

Clerk

By L. S. ROGERS,

Deputy Clerk.

[Endorsed]: Filed Mar. 7, 1945. Lowell Munderff, Clerk. [43]

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## BANKRUPT'S EXHIBIT 7

### Schedule A-3

#### CREDITORS WHOSE CLAIMS ARE UNSECURED

[N. B.—When the name and residence (or either) of any drawer, maker, indorser, or holder of any bill or note, etc., are unknown, the fact must be stated, and also the name and residence of the last holder known to the debtor. The debt due to each creditor

must be stated in full, and any claim by way of set-off stated in the schedule of property.]

						Amount
						Due or Claimed
						\$ Cts.
*	*	*	*	*	*	*
Mildred McDonald,						
617 Irving Street,						
Portland, Oregon.						
Contracted in 1929 re various notes and						
open account as a partner of Lorenzo						
Mansfield doing business as Lorenzo						
Mansfield Studios						2600 00
*	*	*	*	*	*	*

BERNARD G. SHEPHERD  
Petitioner. [44]

United States of America, District of Oregon—ss.

I, G. H. Marsh, Clerk of the United States District Court for the District of Oregon, do hereby certify that the foregoing copy of Schedule A-3 of the schedules in cause No. B-16240, in the matter of Bernard G. Shepherd, bankrupt, in so far as the same relates to Mildred McDonald, a creditor of said bankrupt, has been by me compared with the original thereof, and that it is a correct transcript therefrom and of the whole of such original in so far as the same relates to said creditor, as the same appears of record and on file at my office and in my custody.

In testimony whereof I have hereunto set my hand and affixed the seal of said court at Portland, in said District, this 31st day of January, 1935.

(Seal)               LOWELL MUNDORFF,

Clerk.

By L. S. ROGERS,

Deputy Clerk.

[Endorsed]: Filed June 27, 1931; G. H. Marsh,  
Clerk.

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### CLERK'S CERTIFICATE

United States of America, District of Oregon—ss.

I, Lowell Mundorff, Clerk of the District Court of the United States, for the District of Oregon, do hereby certify: That the foregoing pages numbered from 1 to 44, inclusive, constitute the transcript of record on appeal from an order of said court in a certain bankruptcy cause, No. B26580, in the Matter of Bernard G. Shepherd, Bankrupt, in which said Bernard G. Shepherd is appellant, and Mildred McDonald, now Mildred Muck, is appellee; that said transcript has been prepared by me in accordance with the designation filed by said appellant and in accordance with the rules of court; that I have compared the foregoing transcript with the original record thereof and that the foregoing transcript is a full, true, and complete transcript of the record and proceedings had in said court in said cause, as the same appears of record and on file at my office

and in my custody prepared in accordance with the said designation and rules of court.

I further certify that the cost of the foregoing transcript is \$10.80 and that the same has been paid by the appellants.

In Testimony Whereof, I have hereunto set my hand and affixed the seal of said court, at Portland, in said district, this 8th day of September, 1945.

(Seal)                      LOWELL MUNDORFF,  
Clerk.

By L. S. ROGERS,  
Deputy. [45]

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[Endorsed]:—No. 11140. United States Circuit Court of Appeals for the Ninth Circuit. Bernard G. Shepherd, Appellant, vs. Mildred McDonald, now Mildred Muck, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the District of Oregon.

Filed September 13, 1945.

PAUL P. O'BRIEN,  
Clerk of the United States Circuit Court of Appeals  
for the Ninth Circuit.



United States Circuit Court of Appeals  
for the Ninth Circuit

No. 11140

BERNARD G. SHEPHERD,

Appellant,

vs.

MILDRED McDONALD, now  
MILDRED MUCK,

Appellee.

APPELLANT'S ADOPTION OF STATEMENT  
OF POINTS FILED IN THE DISTRICT  
COURT OF THE UNITED STATES FOR  
THE DISTRICT OF OREGON TO BE RE-  
LIED ON IN HIS APPEAL AND DESIG-  
NATED THE PRINTING OF THE TRAN-  
SCRIPT OF RECORD.

Bernard G. Shepherd, Appellant, hereby adopts for the purposes of this Appeal, the Statement of Points to be relied on as filed in the District Court of the United States for the District of Oregon, and which appear in the Transcript of Record certified to by the District Court of the United States for the District of Oregon and filed in the above-entitled Court.

Appellant hereby designates the entire Transcript of Record to be printed in this Appeal as provided by Subdivision 6, of Rule 19 of the above-entitled Court.

COAN & ROSENBERG,  
RALPH A. COAN,  
Attorneys for Appellant.

(Acknowledgment of Service attached.)

[Endorsed]: Filed Sept. 25, 1945. Paul P.  
O'Brien, Clerk.

In the United States  
**Circuit Court of Appeals**  
For the Ninth Circuit

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BERNARD G. SHEPHERD,  
APPELLANT,

vs.

MILDRED McDONALD, NOW MILDRED MUCK,  
APPELLEE.

---

**BRIEF OF APPELLANT**

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Upon Appeal from the District Court of the United  
States for the District of Oregon.

---

CHRISTOPHERSON & MATTHEWS and  
PAUL M. LONG,  
COAN & ROSENBERG,  
RALPH A. COAN,  
*Attorneys for Appellant.*

W. ELLIS RICHARDSON,  
MOE TONKON,  
*Attorneys for Appellee.*

FILED

NOV 15 1933

PAUL P. O'BRIEN,  
CLERK



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**In the United States**  
**Circuit Court of Appeals**  
**For the Ninth Circuit**

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**BERNARD G. SHEPHERD,**  
**APPELLANT,**

*vs.*

**MILDRED McDONALD, NOW MILDRED MUCK,**  
**APPELLEE.**

---

**BRIEF OF APPELLANT**

---

**Upon Appeal from the District Court of the United  
States for the District of Oregon.**

---

**STATEMENT OF PLEADINGS AND FACTS  
DISCLOSING JURISDICTION OF DISTRICT  
COURT AND CIRCUIT COURT OF APPEALS**

This case arises on an appeal of Bernard G. Shepherd, bankrupt, from an Order of the District Court affirming Referee's Order discharging Bankrupt with

qualifications filed August 1, 1945 (R.\* 36-37). The appeal is taken under Section 24, Bankruptcy Act, 1938; 11 U.S.C.A. Section 47 (R. 37-38). Bernard G. Shepherd was duly adjudged bankrupt by the District Court of the United States for the District of Oregon, December 16, 1941. Specifications of Objections to the Bankrupt's Discharge were filed by Mildred Muck, a creditor (R. 4-9). Bankrupt filed a motion to strike Third Specification of Objection (R. 10), which was denied by Referee's Order dated August 7, 1944 (R. 10). The Referee denied the First and Second Specifications of Objections to Bankrupt's Discharge by Order dated August 28, 1944 (R. 11-12). Objecting creditor did not review Referee's Order. The Referee granted the Bankrupt a qualified Discharge on March 3, 1945, under the terms of which the indebtedness of Mildred Muck was excepted. (R. 28-29). Bankrupt filed a timely petition for review of Referee's Order by the District Court (R. 30-35). The District Court sustained the Referee's Order giving the Bankrupt a qualified Discharge by Order dated August 1, 1945 (R. 36-37). This Appeal is prosecuted from said last mentioned Order.

## STATEMENT OF THE CASE

Bernard G. Shepherd was adjudged Bankrupt by the District Court of the United States for the Dis-

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\*For brevity the Transcript of Record will be referred to herein as "R."

trict of Oregon on December 12, 1941 (R. 14). Mildred Muck was listed as a creditor in the Bankrupt's Schedules and filed her proof of claim in these proceedings which was based on a judgment of the Circuit Court of the State of Oregon for the County of Multnomah dated February 7, 1935 in favor of Mildred McDonald (now Mildred Muck) (R. 45-47, 52-53).

On May 4, 1942 Mildred Muck filed Specifications of Objections to the Bankrupt's Discharge (R. 4-9). These Objections contained Three Specifications and came on for trial before the Referee on August 7, 1944.

The Bankrupt filed a Motion to Strike the Third Specification on the ground that no facts were alleged therein which would authorize or permit the denial of a discharge (R. 10). The Referee denied this Motion (R. 10).

After a trial of the issues raised by the First and Second Specifications the Referee denied and disallowed both of said Specifications and took the Third Specification under advisement (R. 11-12).

On the 3rd day of March, 1945, the Referee filed his Opinion in which he held and ruled that the Third Specification of Objection should be sustained so far as the claim of Mildred Muck was concerned and that the Bankrupt was only entitled to a qualified discharge from which the judgment owing the objecting

creditor, Mildred Muck, should be excluded (R. 12-28).

The Referee entered a Qualified Order of Discharge excepting therefrom the judgment due Mildred Muck which had been duly proved and allowed in this bankruptcy proceeding (R. 28-29).

The Bankrupt promptly reviewed the Referee's Order last referred to by a Petition to Review filed March 7, 1945 (R. 30-35). The District Court adopted the Referee's Opinion and affirmed the Referee's Order in a Memorandum of Decision dated and filed July 31, 1945 (R. 36), and on August 1, 1945 the District Court made and entered an Order Adopting the Referee's Opinion as the Opinion of the District Court, affirming the Referee's Order discharging the Bankrupt with qualifications (R. 36-37).

This Appeal is prosecuted from the Order of the District Court which affirms the Referee's Order and denies a Discharge to Bankrupt on the judgment of Mildred Muck.

The facts are clear and undisputed and are fully set forth in the Referee's Opinion.

There is only one question involved which is raised by the Third Specification of Objection. This question is:

May one who is indebted upon a judgment obtained upon a debt or obligation previously scheduled in a prior bankruptcy proceeding, and which indebtedness was discharged in the prior bankruptcy proceedings, the judgment being ob-

tained subsequent to the discharge in the prior bankruptcy proceedings by reason of a new promise made by the Bankrupt, schedule such judgment in a subsequent bankruptcy proceeding filed more than six years after the discharge in his first proceedings, and be granted, and obtain, a discharge in the second bankruptcy proceedings from such judgment?

As stated by the Referee in his opinion, this question appears to be one of first impression under the Bankruptcy Act, and one that has never been passed upon by any court.

## **SPECIFICATIONS OF ERROR**

1. The District Court erred in finding and holding that the debt owing by the Bankrupt to Mildred Muck, being a judgment entered against the Bankrupt on the 7th day of August, 1935, and scheduled by the Bankrupt in his voluntary petition, is the same debt as a debt owing to Mildred McDonald, now Mildred Muck, and scheduled in the Bankrupt's petition in bankruptcy filed June 27, 1931.

2. The District Court erred in finding and holding that the Bankrupt waived his right to a discharge in the present bankruptcy proceedings from a judgment obtained by Mildred Muck on the 7th day of August, 1935, based upon a new promise to pay the indebtedness from which Bernard G. Shepherd was discharged

in his bankruptcy proceedings filed June 27, 1931.

3. The District Court erred in finding and holding that Bernard G. Shepherd, Bankrupt herein, was not entitled to a discharge from the indebtedness owing Mildred Muck which was duly scheduled in these proceedings for the reason that the Bankruptcy Act of the United States expressly provides that a bankrupt is entitled to a discharge from all his provable debts unless he has committed one or more of the acts enumerated in Section 14 (c) of the Bankruptcy Act.

4. The District Court erred in finding and holding that the Bankrupt was not entitled to a discharge from the indebtedness owing Mildred Muck duly scheduled, proved and allowed in these proceedings.

5. The District Court erred in refusing to sustain Bankrupt's motion to strike the third specification of the objection filed by Mildred Muck, objecting creditor, in opposition to Bankrupt's discharge.

6. The District Court erred in finding and holding that Bernard G. Shepherd, Bankrupt, was not entitled to and could not seek a second discharge from the same obligation owing Mildred McDonald, now Mildred Muck, as that scheduled in his first bankruptcy proceeding filed June 27, 1931.

7. The District Court erred in finding and holding that to grant a discharge in this proceeding from the indebtedness owing Mildred Muck would be an abuse of process and an imposition on the Court for the rea-



son that a Bankrupt is entitled as a matter of right under the Bankruptcy Act to a discharge from all provable debts unless he has committed one of the acts set forth in Section 14 (c) of said Act.

8. The District Court erred in entering a qualified and restricted order of the discharge instead of granting Bankrupt a complete and full discharge from all his provable debts.

9. The District Court erred in finding and holding that Bankrupt waived all rights under the Bankruptcy Act to at any time whatsoever obtain a discharge upon the indebtedness of Mildred Muck by making a promise to pay said indebtedness subsequent to the discharge entered in Bankrupt's first bankruptcy proceedings.

10. The District Court erred in finding and holding that the Bankrupt had no right to schedule in this proceeding an indebtedness due and owing Mildred Muck because said indebtedness was discharged in his former bankruptcy proceeding.

11. The District Court erred in finding and holding that the new promise made by Bankrupt to pay the indebtedness of Mildred Muck theretofore discharged in his bankruptcy proceedings of June 27, 1931, made said indebtedness and any judgment obtained thereon a non-dischargeable debt in any valid bankruptcy proceedings filed by or against the Bankrupt at any time thereafter.

12. The District Court erred in entering an order adopting the opinion of the Referee as the opinion of the District Court and in affirming the order of the Referee discharging the Bankrupt with qualifications.

## POINTS AND AUTHORITIES

### POINT I

**(a) Bankrupt entitled to a discharge as a matter of law.**

Bankruptcy Act. Section 14; 11 U.S.C.A. Sec. 32.

Bankruptcy Act, Section 17; 11 U.S.C.A. Sec. 35.

In re Jacobs, 241 F. 620; 39 A.B.R. 385.

Hardie vs. Dry Goods Co., 165 F. 588; 20 L.R.A. (N.S.) 785.

Remington on Bankruptcy, Fifth Ed., Chap. L, Vol. 7, Pg. 399.

Remington on Bankruptcy, Fifth Ed., Sec. 3219, Vol. 7, Pg. 455.

Remington on Bankruptcy, Fifth Ed., Sec. 3516, Vol. 7, Pg. 768.

Williams v. U. S. F. & G. Co., 236 U.S. 549; 35 S. Ct. 289; 59 L. Ed. 713.

**(b) The doctrine of Res Judicata does not apply to the facts in this case.**

Remington on Bankruptcy, Fifth Ed., Sec. 3457, Vol. 7, Pg. 714.

30 Am. Jur. Sec. 172, Pg. 914.

30 Am. Jur. Sec. 180, Pg. 925.

30 Am. Jur. Sec. 201, Pg. 940.

Bankruptcy Act, Sec. 17; 11 U.S.C.A. Sec. 35.  
Collier on Bankruptcy, Fourteenth Ed. Sec.  
17.28, Vol. 1, Pg. 1657.  
Supplement to Moore's Collier, Fourteenth Ed.  
under Sec. 17.28.  
Local Loan Company v. Hunt, 292 U.S. 234; 78  
Law. Ed. 1230; 24 A.B.R. (N.S.) 668.  
In re: Bybee, 124 Fed. 1011.  
Matter of Charles S. Baker, 275 Fed. 511; 47  
A.B.R. 255.  
Matter of Dierck, 37 A.B.R. (N.S.) 198.  
Prudential Loan & Finance Co. v. Roberts, 52  
Fed. (2) 918.  
Bluthenthal v. Jones, 208 U. S. 64; 52 L. Ed.  
390.

## POINT II

**The making of a new promise to pay a debt discharged in a prior bankruptcy proceeding is not a waiver to the right to thereafter schedule in a subsequent bankruptcy proceeding, a judgment based on the new promise and be discharged therefrom.**

Remington on Bankruptcy, Fifth Ed., Sec.  
3499.50, Vol. 7, Pg. 756.  
67 C. J. Sec. 1, Pg. 289.  
67 C. J. Sec. 4, Pg. 299.

## POINT III

**A Judgment based on a new promise to pay a debt theretofore discharged in bankruptcy is a new indebtedness and is not the same indebtedness as the one formerly discharged.**

Matter of Cox, 47 A.B.R. (N.S.) 668; 33 Fed. Sup. 796.

8 Corpus Juris Seccondum, Sec. 583<sup>3</sup> (d), Pg. 1577.

Wolffe v. Eberlein, 74 Ala. 99; 49 Am. Rep. 809.

Mathewson v. Nedham, 81 Kan. 340; 105 Pac. 436; 26 L.R.A. (N.S.) 274.

6 Am. Jur. 535.

Holden v. Chamberlain, 46 N. D. 353; 179 N. W. 706.

Bluthenthal v. Jones, 208 U. S. 64; 52 L. Ed. 390.

U. S. National Bank of LaGrande v. Miller, 118 Or. 280; 246 Pac. 726.

## ARGUMENT

### POINT I

Under this point, we will direct the argument to cover specifications of error 3 to 8 inclusive and specifications of error 11 and 12. Each of these specifications present similar questions of law and will therefore be considered together.

In order that the court may have the bankrupt's position clearly presented, Section 14 and Section 17 of the Bankruptcy Act appear in full in the Appendix A-1.

It will be readily seen from a reading of sections 14 and 17 of the Bankruptcy Act that a bankrupt is entitled to a discharge, as a matter of right, and it is the absolute duty of a court sitting in bankruptcy to grant this right to a bankrupt in accordance with the

provisions of Section 14, unless it is made to appear to the satisfaction of a court that the bankrupt has violated some one of the provisions of sub-section (c) of Section 14.

The right to a discharge in bankruptcy is absolutely guaranteed to an honest bankrupt. This right is a most precious one, involves the happiness and security of not only the bankrupt himself, but the welfare and prosperity of the community in which he lives.

It is a right that the United States Courts have uniformly held to be inviolate and enforceable, unless the bankrupt, by reason of dishonest conduct, or failure to obey the court's orders, has, himself, forfeited it.

The very terms of the statute disclose the intention of Congress in this regard. The words used in the statute are *must* and *shall*; these words leave little discretion in a given case where the facts do not clearly bring the bankrupt within the provisions of those exceptions which are embodied within the Act, itself.

Remington on Bankruptcy, in his Fifth Edition, Chapter L. Vol. 7 beginning at Page 399, discusses the question of discharge at great length, and points out that, while, originally, bankruptcy laws were enacted principally for the benefit of creditors, that, as time went on, it was determined that the interests of

the public could best be served by granting discharges to honest bankrupts to rehabilitate one who, through misfortune, has become indebted, and, unless relieved therefrom, would become a virtual charge upon the community.

Thus, the various bankruptcy acts of the United States have become more and more liberal in the granting of discharges. Congress has granted more and more relief to insolvent debtors by greatly extending the scope of the Bankruptcy Act, all in the public interest, until, today, bankruptcy is no longer considered dishonorable, but is known to be a means granted to the people of the United States to enable unfortunate, harassed, but honest men to get a new start in life, and to become again useful, productive and honorable citizens.

The courts have repeatedly stated that the right given to secure a discharge by the Bankruptcy Act should be liberally construed.

In the case of *In Re: Jacobs* 241 F. 620, 39 A. B. R. 385 (C. C. A. Ohio), the court said:

"The language giving the right to secure a discharge in bankruptcy ought, therefore, to be liberally construed.

"Indeed, where an application for a discharge is seasonably filed in a District Court, the Judge of the court is 'bound to grant it unless upon investigation' it appears that the bankrupt has 'committed one of the six offenses which are specified' in Section 14b."



Again, we find similar expressions in the case of *Hardie v. Dry Goods Co.*, 165 F. 588, 21 A. B. R. 457, 20 L.R.A. (N.S.) 785 (C.C.A. Tex.):

“Originally, in bankrupt laws, the discharge of the bankrupt may have been incidental, and the main purpose the equal distribution of his goods among creditors; but to say it now, and of the present law, we must shut our eyes to the actual practice in our courts. In nearly all and every voluntary bankruptcy brought under the present law the administration or distribution of the bankrupt’s property has been practically concluded before filing petition, and the sole object of the petitioner is to be relieved of his debts, and in number the voluntary cases are about four to one of the involuntary. (See Report, Dept. of Justice, 1907). And the same may be said of the voluntary cases under the Act \* \* \* 1867, \* \* \* which was passed mainly to relieve the unfortunate debtors ruined by and through the vicissitudes of the great Civil War.

“For these considerations, we are disposed to deny that in the present bankruptcy law the discharge of the honest debtor is a mere incident which could have been omitted without impairing its symmetry and efficiency; and, on the contrary, to assert that the release of the honest, unfortunate, and insolvent debtor from the burden of his debts and his restoration to business activity, in the interest of his family and the general public, are the main, if not the most important, objects of the law.”

We quote further from *Remington on Bankruptcy*, Fifth Edition, Sec. 3219, Vol. 7, P. 455.

“Section 3219. Unless Bankrupt Commits One of Acts Prohibited His Discharge ‘Shall’ be Grant-

ed.—Unless the bankrupt has committed some one or more of the acts prohibited by the Bankruptcy Act, his discharge ‘shall’ be granted. And Section 14 (c), 11 U.S.C.A. Section 32 (c) prescribed what acts will bar discharge.”

All provable debts, except those that are expressly excepted by the Bankruptcy Act, are discharged.

Remington On Bankruptcy, Fifth Edition, Section 3516, Volume 7, Page 768

where the author says:

“Section 3516. Dischargeability of All ‘Provable’ Debts, Except Those Excepted. — All provable debts, demands and claims, whether allowable in full or in part, are discharged, except those especially excepted by Section 17 (a) of the act, 11 U.S.C.A. Section 35 (a), and debts, demands and claims not provable, are not discharged \* \* \* .”

In view of the express provisions of the Bankruptcy Act, considering the many expressions of our courts on the question of the right to a discharge guaranteed to an honest bankrupt, remembering the express intention of Congress in liberalizing and extending the beneficial provisions of this Act to include farmers, corporate reorganizations and similar provisions, it is submitted that no court should, without compelling reasons, and in the most clear-cut cases, deny to a bankrupt a discharge which, after all, is the most important right and the one purpose and object which has actuated Congress in the enactment of bankruptcy legislation.

Let us then consider the facts in this case.

It is conceded that the third specification of objection in this case does not set forth any of the prohibited provisions enumerated in sub-division (c) of Section 14 of the Bankruptcy Act.

At the hearing before the Referee, the Bankrupt filed a motion to strike the third specification of objection, on the ground that there were no facts set forth therein which were sufficient to sustain an order denying the Bankrupt his discharge (R. 10).

This motion was denied by the Referee (R. 10), and the order entered by the Referee denies the bankrupt a discharge of the debt of the objecting creditor (R. 28-29), although there is no evidence in the record, nor are there any facts stated by the Referee in his opinion, which could, under the provisions of the Bankruptcy Act, deny the bankrupt his discharge. This order of the Referee was affirmed by the District Court (R. 36-37).

The Referee, in his opinion, which has been adopted by the District Court (R. 36)\*, states that the facts in this case are analogous to a situation where a bankrupt, prior to the enactment of the present Bankruptcy Act, known as the Chandler Act, failed to apply for a discharge within the time limited by the former Act, or disobeyed the orders of the

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\*Wherever the argument mentions Referee's opinion, it also includes the opinion of the District Court.

court in failing to pay the cost of the proceedings.

Many caess are cited to support this rule.

The writer of this brief has no quarrel or disagreement with any of the cases cited in this connection. Most of the cases have become of no force or effect by reason of the fact that the Chandler Act, by its express terms, makes it the duty of the court to grant the bankrupt a discharge on its own motion, unless it is found that some of the acts prohibited in Section 14 have been committed by the bankrupt.

Here again we find an instance of the intention of Congress in protecting, guaranteeing and aiding an honest bankrupt in obtaining a discharge.

It is pointed out in this opinion that many of the cases adhered to the rule of denying a bankrupt a discharge because he had failed to apply for the same within time, even though his failure was due to the neglect, or, sometimes, the dishonorable conduct of his counsel, the Referee concluded, therefore, that if the courts, in these hard cases, adhere strictly to the rule announced that, certainly, in a case such as is now before this court, this court should depart from the express provisions of the Bankruptcy Act and find a reason why the bankrupt in this case should be denied a discharge, no matter what hardship may result therefrom.

We cannot follow this reasoning. There is no contention here that Bernard G. Shepherd has not com-

plied in every particular with the orders of this court, has not fairly and honestly disclosed all of his indebtedness, has not promptly paid into the registry of this court all costs and expenses required of him to be paid, or has not fully accounted for all his property.

Certainly, neither the Referee, nor the objecting creditor, have found or produced any fact showing that this Bankrupt is not an honest man, has not fully complied with the Bankruptcy Act, and he should, therefore, be entitled to a discharge.

In this connection, we wish to quote from a case referred to in the Referee's opinion, and which shows the attitude of the court, even of the Supreme Court of the United States.

In *Williams vs. United States F. & G. Co.*, 236 U. S. 549; 35 S. Ct. 289; 59 L. ed. 713; the Supreme Court of the United States said on Page 716 L. ed.:

"It is the purpose of the bankrupt act to convert the assets of the bankrupt into cash for distribution among creditors, and then to relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes. *Wetmore v. Markoe*, 196 U. S. 68, 77, 49 L. ed. 390, 394, 25 Sup. Ct. Rep. 172, 2 Ann. Cas. 265; *Zavelo v. Reeves*, 227 U. S. 625, 629, 57 L. ed. 676, 678, 33 Sup. Ct. Rep. 365, Ann. Cas. 1914D, 664; *Burlingham v. Crouse*, 228 U. S. 459, 473, 57 L. ed. 920, 926, 46 L.R.A. (N.S.) 148, 33 Sup. Ct. Rep. 564. And nothing is better settled than that statutes should be sensi-



bly construed, with a view to effectuating the legislative intent. *Lau Ow Bew v. United States*, 144 U.S. 47, 59, 36 L. ed. 340, 344, 12 Sup. Ct. Rep. 517; *Re Chapman*, 166 U. S. 661, 667, 41 L. ed. 1154, 1158, 17 Sup. Ct. Rep. 677."

The Referee holds that, because the Bankrupt once obtained a discharge in bankruptcy from an indebtedness owing the objecting creditor, which he waived by making a new promise to pay it, and which later was used as the basis of obtaining the judgment scheduled in the present proceedings and having been accorded relief in his first bankruptcy proceedings from oppressive obligations arising from business misfortunes, he thereby waived his right to any relief in bankruptcy on this obligation and indebtedness forever.

It is respectfully submitted that, if this doctrine is to be adopted by our courts, much of the beneficial relief, which is the manifest purpose of the Act, will be denied to honest debtors. No one would contend that it was not an honest and honorable act for one who had been discharged in bankruptcy from an indebtedness, to later, when he found himself able, agree to pay the indebtedness, even though not legally bound so to do. This is not a dishonest act; it is, on the contrary, a most honorable one, but life is full of many disappointments and manifold misfortunes. A man may be prosperous today, have high expectations, believe himself capable of great things. Tomorrow, adversity strikes him, and he finds himself unable to



carry out his good intentions and his rosy promises. Is such a one to be denied relief, simply because he had misfortune more than once? Many honorable men have been forced into bankruptcy through sickness or misfortune on two, nay, three and four occasions. In fact, the Bankruptcy Act expressly provides that one may avail himself of its provisions for a discharge once every six years. If it were the intention of Congress that a person could only once have the benefit of a discharge in a case like the one here presented, the law would so expressly provide.

The Bankrupt, in this case, did obtain a discharge in 1931. He later promised to pay Mildred McDonald, now Mildred Muck. She promptly sued him and obtained the present judgment, and with this weapon she harassed him at every opportunity, made it impossible for him to keep a position or to obtain the money with which to carry out his new promise. Nay, he was probably more unfortunate after this judgment was obtained than he was at the date of his first adjudication. Is he to be left forever without the benefits of an act which expressly provides that he can apply for relief a second time at the end of six years?

Is there any difference between this judgment and other new indebtedness incurred by this Bankrupt after his former discharge, so far as the effect upon his future, his ability to earn a livelihood, or his becoming a public charge, all of which, as we have here-

tofore stated, are the underlying reasons for the enactment of this legislation.

The Referee finds, and states in his opinion, that, because Bernard G. Shepherd once obtained from this court a discharge upon the indebtedness of Mildred Muck, formerly Mildred McDonald, in a bankruptcy proceeding in 1931, he is imposing upon this court by asking a discharge in this proceedings from a judgment granted long after the first discharge by reason of his promise to pay this obligation and the Referee finds that to permit him to obtain a discharge in this proceeding would be an abuse of process, as well as an imposition upon this court.

We respectfully submit that there is nothing in this record, nor is there anything to be found in any of the cases cited by the Referee in his opinion, which should lead this court to any such conclusion.

It is true that in some of the decisions cited by the Referee the courts have said that where a bankrupt had scheduled indebtedness in a bankruptcy proceeding and had failed to obtain a discharge therefrom, that to file a subsequent proceeding, in which the same debts were scheduled, and again pray for a discharge on these debts, would be an imposition upon the court and an abuse of process. But, in all of these cases we find that the bankrupt had failed to obey the court's orders, or had committed some dishonest act, which deprived him of the right to a discharge. In such case, a bankrupt, by filing a second petition

and listing the same indebtedness, was, of course, attempting to circumvent the plain provisions of the Bankruptcy Act, or was, in effect, saying to a court: True, I have refused to obey the orders of this court in a prior proceeding, I have failed to pay the costs in the prior proceedings, although requesting relief, and now I wish to obtain those benefits which I either was not entitled to as a matter of law, or of which I deprived myself by failing to obey the court's orders.

This is a far different situation than the one presented by the record in this case.

### **RES JUDICATA DOES NOT APLY IN THIS CASE**

The Referee states, in his opinion, that the cases which deny to a bankrupt a discharge in subsequent bankruptcy proceedings from debts scheduled in a prior proceeding, in which a discharge was denied, are based upon the doctrine of *res judicata*. These cases do proceed upon this theory, and most of them rest their decisions upon this doctrine. We submit that the facts in this case are not in any way analogous to the facts in any of the cases cited by the Referee in his opinion or relied upon in reaching the conclusions of law therein set forth.

The Bankruptcy Courts, in passing on this question and laying down the above mentioned rule, have proceeded on the theory that a petition for a dis-

charge is an independent legal proceeding and when properly raised and determined by a Bankruptcy Court that the decision becomes *res judicata* in all subsequent proceedings by the bankrupt and his privies in relation to the facts so determined. Remington on Bankruptcy, Fifth Edition, Sec. 3457, Vol. 7, P. 714.

In relying upon the doctrine of *res judicata* as conclusive on the above mentioned issue of the effect of the denial of a discharge in former bankruptcy, the Courts have gone no farther than to say that the denial of a discharge has the effect of a judgment on the issues before such Court, that is, either failure to timely apply for a discharge, which is construed as giving rise to a default judgment, or the trial of specific objections based upon some one of the acts prohibited in Section 14 of the Act, and a determination by the court that the bankrupt was not entitled to a discharge.

Manifestly, the only issue determined in such a proceeding is whether or not the bankrupt in *that* proceeding was entitled, as a matter of right, on the then existing facts, to a discharge.

The Referee, in referring to the doctrine of *res judicata* in connection with the third specification of objection, may, perhaps, refer to the judgment of the Circuit Court of Multnomah County, Oregon, which gave to Mildred Muck her judgment, now scheduled in this proceeding.

The doctrine of *res judicata* is well recognized, but, of course, is subject to very definite limitations.

Let us see what the Courts have generally laid down as the meaning and extent of the doctrine of *res judicata*.

In Vol. 30, *American Jurisprudence*, the text defines the term as follows:

"A final judgment rendered by a Court of competent jurisdiction, on the merits, is conclusive as to the rights of the parties and their privies, and as to them constitutes an absolute bar to a subsequent action involving the same claim, demand, and cause of action. If, however, the two suits do not involve the same claim, demand and cause of action, such effect will not be ordinarily given to the prior judgment. In this respect, it is worthy of notice that there must be not only identity of subject matter, but also of the cause of action, so that a judgment in a former action does not operate as a bar to a subsequent action, where the cause of action is not the same, although each action relates to the same subject matter." 30 *Am. Jur.*, Sec. 172, Pg. 914.

The text goes on in a subsequent section and says:

"The rule granting conclusiveness to a judgment in regard to issues of fact which could properly have been determined in the action is limited to cases involving the same cause of action. Where a second action is upon a different claim, demand, or cause of action, the established rule is that the judgment in the first action operates as an estoppel only as to the points or questions actually litigated and determined, and not as to matters not litigated in the former action, even though such matters might properly have been deter-



mined therein. Accordingly, before the doctrine of *res judicata* is applied in such cases, it should appear that the precise question involved in the subsequent action was determined in the former action. These rules prevail whether the judgment is used in pleading as a technical estoppel, or is relied on by way of evidence as conclusive *per se*." 30 Am. Jur., Sec. 180, Pg. 925.

The rule is stated in Section 201, Am. Jur., as follows:

"In order that a judgment may operate as a conclusive determination of a cause of action, or of facts litigated therein, it is necessary that it should have been rendered by a court of competent jurisdiction of the parties and of the subject matter. The fact that a person invokes the jurisdiction of a court does not preclude him for questioning its jurisdiction of the subject matter when its judgment is asserted as *res judicata*. On the other hand, the fact that a person attacks the jurisdiction of a court does not exempt him from the operation of the judgment under the doctrine of *res judicata*."

If, therefore, it is contended in the instant case that the judgment of the Circuit Court of Multnomah County, Oregon, in favor of Mildred Muck and against the bankrupt is conclusive on the subject of the dischargeability of such judgment in a subsequent bankruptcy of the judgment debtor, it must be made to appear that this issue was not only raised and determined by the Circuit Court, but also that the Court had jurisdiction to pass upon that question.

It must be conceded that the Circuit Court of Multnomah County, Oregon, did not have before it



any such issue as this. In fact, no such issue then could have been raised because the facts to support such an issue did not exist.

Further than this, *and much more vital*, is the fact that the Circuit Court of Multnomah County, Oregon had no jurisdiction whatever to grant or to deny of a discharge in bankruptcy to Bernard G. Shepherd in any proceeding.

It has, of course, been held so many times that the jurisdiction of a bankruptcy court is exclusive in reference to all matters arising in a bankruptcy proceeding itself that it is not necessary to cite authority to support this statement.

Referring again to the provisions of the Bankruptcy Act quoted in this Brief, it might be well to point out that the granting or denial of a discharge in bankruptcy is the exclusive province of a Bankruptcy Court made so by the provisions of the Act, Section 14.

Section 17 of the Act, Appendix A-1, deals with debts which are not affected by a discharge and, generally speaking, it is the province of a State Court to pass on the question of dischargeability of a particular debt.

Therefore, in the instant case it became the province of the Circuit Court of Multnomah County, Oregon to pass on the question as to whether or not the debt of Mildred Muck was an enforceable one when

the question was raised in that forum. In passing upon this issue, the Circuit Court determined that the former adjudication had been waived by the making of a new promise, and that is all it did, or could decide.

Collier on Bankruptcy, 14th Ed., Vol. 1, Sec. 17.28, Pg. 1657, discusses the question as to what Court determines the effect of a discharge and says that, ordinarily, it is for the State Court and not the Federal Bankruptcy Court to determine the effect of a discharge. The Federal, or Bankruptcy Court, has the exclusive right to determine whether a discharge shall be granted or denied, but ordinarily the Bankruptcy Court does not have jurisdiction nor does it assume to pass upon the question as to whether a particular debt has been discharged.

It is only in exceptional cases where a Bankruptcy Court proceeding under its equitable jurisdiction has undertaken to pass on this question.

In the Supplement to Moore's Collier, 14th Ed., under Sec. 17.28, the author discusses this question at length, referring to the cases dealing with this question, and among other things the author says:

"The Courts, however, have in almost every instance denied these attempts and several notable opinions have emphasized the general rule stated in the Treatise; that the bankruptcy court merely determines the *right* to a discharge but does not, and except in certain circumstances hereinafter mentioned, should not determine the *effect* there-

of, which is properly adjudicated in the non-bankruptcy forum when the creditor sues on his claim and the bankrupt pleads his discharge as a defense."

The text discusses the cases, especially *Local Loan Company vs. Hunt*, 292 U. S. 234, 24 A. B. R. (N.S.) 668, that case having been decided on the ground of exceptional hardship to a bankrupt.

Most of the cases dealing with this subject have reached the conclusion that the Bankruptcy Court should not in any way interfere with or attempt to relitigate proceedings had in a State Court, the subject matter of which was the question of the dischargeability of a particular debt.

In all of these cases, the court has carefully pointed out that it is the province of the State Court, either under the express provisions of Section 17 of the Act, or in considering whether or not a former discharge was waived by a new promise, to determine whether or not a particular indebtedness is in fact discharged by a prior bankruptcy proceeding.

On the other hand, the Courts have been equally emphatic in holding that a State Court had no jurisdiction or power to determine the question of whether or not the bankrupt should obtain a discharge, that question being exclusively reserved to and vested in a Bankruptcy Court.

As an illustration of this doctrine, we cite the case of *In re: Bybee*, 124 Fed. 1011 (Dist. Ct. N.D.

Cal., 1903) in which the Court *held* that the denial of a discharge upon a particular debt in a State Court insolvency proceeding was not *res judicata* and binding upon the bankruptcy court where it was later scheduled by the bankrupt.

In other words a claim, simply because of a denial of a discharge thereon in one proceeding, does not thereby become charged with *non-dischargeability forever*.

Another case based on this subject is *Matter of Charles S. Baker*, 275 Fed. 511; 47 ABR 255 (U. S. Dis. Ct. S.D., N.Y., Sept., 1921).

In this case, one Baker was adjudged a bankrupt in 1910 and discharged in 1911. In this proceeding, he failed to schedule a note in the sum of \$281.10. Thereafter the creditor holding the note obtained a judgment thereon. More than six years thereafter, Baker filed a second petition in bankruptcy and scheduled the judgment.

It was contended that since the debt was not scheduled in the first bankruptcy proceeding, and therefore the discharge in that proceeding did not affect it, that it was *non-dischargeable* in the second bankruptcy proceeding. The Court, however, overruled this contention and said, at Page 512:

“The only effect of failure to schedule is that an otherwise dischargeable debt is not discharged. Thereafter, the creditor may pursue his remedies unaffected by the discharge. When, however, more

than six years later, a new petition is filed, the bankrupt may schedule every outstanding debt, and be discharged in respect of a debt still existing, which had been omitted from the schedules of the first bankruptcy.

“Failure to schedule and consequent failure to discharge a particular debt does not operate to adjudicate that the debt is not dischargeable. There is no *res adjudicata* doctrine, because nothing had been adjudicated so far as affects an unscheduled debt. If a discharge is refused, then, of course, that refusal is *res adjudicata*, but, such is not this case. Cases cited by the attorney for the creditor are those where either (1) a discharge was previously refused or (2) where a previous petition in bankruptcy is still pending. Of course, where there is a refusal to discharge, the adjudication necessarily is that for the same reason justified by the statute the bankrupt cannot obtain a discharge of any of his debts.

“Where there is a previous proceeding pending, obviously the court will not entertain a second proceeding, so far, in any event, as affects debts existent at the time of filing the petition in the first proceeding. The case at bar, however, is different. Here the bankrupt did no act to bar his previous discharge and the effect of failure to schedule was merely to let the debt remain alive. When, therefore the bankrupt after six years seeks a discharge upon a new petition, the act contemplates that he may be discharged of any then existing debts.”

Here again it will be readily seen that the doctrine of *res judicata* can only come into play where the Court denying the discharge or granting the discharge, as in this case, had before it for determination an issue on the very claim in question.



In the case of Matter of Dierck, 37 ABR (N.S.) 198 (U.S.D.C. S.D. N. Y. Apr., 1938), the Court held that where a bankrupt had omitted a claim from his schedules in his first proceedings and thereafter filed a second proceeding in which he scheduled the debt, but was unable to obtain a discharge in the second proceedings because the six years limitation had not elapsed, he could thereafter file a third proceeding and schedule the debt and a discharge would be good thereon.

The Court, in passing on this question, said on Page 199:

“A debt omitted from schedule in a bankruptcy proceeding and for that reason not touched by the discharge obtained there may be discharged in a later proceeding in which application for discharge is made more than six years after the first discharge. *In re Baker* (D.C., N. Y.), 47 Am. B. R. 255, 275 F. 511; *In re Lyons* (D.C., N. Y.) 2 Am. B. R. (N.S.) 552, 287 F. 602; Remington on Bankruptcy, section 3585. Such a case is quite different from one where the debt was listed in the earlier proceeding but the bankrupt failed to apply for discharge or was denied discharge in that proceeding and then seeks to get a discharge from the same debt in a later proceeding, as in *In re Feigenbaum* (C.C.A., 2nd Cir.) 9 Am. B. R. 595, 121 F. 69, and similar cases. See *In re Zeiler* (D.C., N.Y.), 33 Am. B. R. (N. S.) 627, 18 F. Supp. 539. It follows that while the debt due the dairy company survived the discharge in the first bankruptcy, it did not thereby acquire a permanently non-dischargeable character.

“The second proceeding was altogether futile so far as discharge from debts was concerned be-



cause any application for discharge that might have been made in it would necessarily have been within the prohibited six years period. Under the circumstances, failure to get a discharge in that proceeding did not render this debt *bankruptcy-proof forever*."

In the case of *Prudential Loan and Finance Company vs. Roberts*, 52 Fed. (2nd) 918 (C.C.A. 5th Cir. Oct., 1931) one Roberts was adjudicated a voluntary bankrupt in July, 1922, and was discharged in August, 1923. In February, 1926, he executed a note to Prudential Loan and Finance Company. In March he filed a second voluntary petition and scheduled this note. In April, 1927, he gave the Prudential Loan and Finance Company a new note upon which a judgment was entered in June, 1927. Roberts did not apply for a discharge on his second bankruptcy, but in December, 1929 filed a third petition, and in this third petition filed a petition for a discharge. All of these bankruptcy proceedings took place in the same court.

The Prudential Loan and Finance Company contended that since the debt upon which the judgment was later entered was scheduled in the 1927 bankruptcy in which no discharge was obtained that it could not be discharged in the second bankruptcy because of the doctrine of *res judicata*.

The Court, after quoting from the decision of *Bluthenthal vs. Jones*, 228, 208 U. S. 64; 52 L. Ed. 390 *held* that under the facts in that case the discharge, in the third proceeding, should be granted over the

objections of the Prudential Loan and Finance Company.

The court used the following language on Page 919:

“The peculiarity of the case at bar which distinguishes it from others heretofore decided is that on looking to the records in the same court of Roberts’ prior bankruptcies it is apparent that in the bankruptcy of 1927 there was an insuperable obstacle to a discharge, in that he had obtained a discharge in bankruptcy within six years prior to April 1, 1928, the last day on which he might make application. Title 11, U.S.C. Sec. 32 (a), and (b) (5), 11 U.S.C.A. 32 (a) and (b) (5). Had he applied, the discharge must necessarily have been denied for this reason, and we think this is the only thing that can on the facts shown by the record be fairly considered to be adjudicated by the default in not applying. Manifestly, the mere adjudication that Roberts was not on April 1, 1928 entitled to a discharge because six years had not elapsed since his last discharge on August 23, 1923, could not prove him disentitled on November 29, 1929. The refusal of a discharge because of a prior discharge within six years stands on a different footing from a refusal on any other ground set forth in title 11, U.S.C., 32 (b), 11 U.S.C.A. 32 (b). The other grounds all involve reprehensible conduct of the bankrupt which Congress intended to punish by a perpetual refusal to discharge him from the claims of his then creditors. The purpose in adding the ground relating to a prior discharge within six years was not to punish, but only to postpone a second discharge for that period of time. An ill-advised voluntary, adjudication, or an involuntary one on acts of bankruptcy which do not also defeat discharge, had within five years

of the granting of a prior discharge, and on which no discharge can possibly be granted, was not intended to result in making the provable claims of creditors *bankruptcy-proof forever*. *Such a construction would tend to defeat one of the main purposes of the act, to wit: The relief of honest debtors who surrender their property to their creditors.*" (Italics ours)

All of the above cases show how limited is the doctrine of *res judicata* on the subject of a discharge and that to enable this doctrine to be applied in a given case it must clearly appear that a Bankruptcy Court of competent jurisdiction actually passed upon the question of discharge in a given case.

The opinion of the Referee in this case has the effect, if his order is sustained, to make the indebtedness of Mildred McDonald a new class of indebtedness, not covered by any of the provisions of the Bankruptcy Act. It makes the claim of Mildred McDonald a non-dischargeable debt from the date of the new promise, and, in effect, adds to, and enlarges, the provisions of Section 17 of the Act.

In view of the decisions last quoted above, and of the mandate of the Act, itself, it must clearly appear that such a holding by this court would, in the language of the Supreme Court of the United States, *Bluthenthal vs. Jones*, *supra*, "defeat one of the main purposes of the Act to wit: The relief of honest debtors who surrender their property to their creditors."

The facts in the case at bar disclose that two

courts have dealt with the indebtedness of the objecting creditor, prior to the adjudication of the Bankrupt in these proceedings. The first court was the District Court, sitting in bankruptcy and dealing with the adjudication of this Bankrupt in 1931. In this proceeding, that court passed upon the question as to whether or not the indebtedness of Mildred McDonald, the present objection creditor, was a dischargeable obligation. The court determined that question in favor of the Bankrupt, and granted him a discharge. The second court to pass upon, or deal with, this obligation was the Circuit Court of Multnomah County, State of Oregon. That court held that Bernard G. Shepherd, Bankrupt in this proceeding, had, by a new promise, waived his defense of the discharge in his first bankruptcy proceeding, and entered a judgment against him.

The Referee, in his decision, upon which the order complained of here is based, uses the doctrine of *res judicata* as a basis for his opinion and order.

Out of which proceeding the *res judicata* relied upon by the Referee arose is not stated in his opinion. Either horn of the dilemma which confronts the objecting creditor in these proceedings, if the doctrine of *res judicata* is to be relied upon to support the Referee's order, must inevitably lead to a determination that the Referee's order is erroneous.

If the judgment relied upon is the judgment of the District Court in granting a discharge in the bank-

ruptcy proceedings of 1931, then the result is that the doctrine of *res judicata* is beneficial to the Bankrupt and not to the objecting creditor, because that judgment holds that this is a dischargeable debt. It has never been modified or overruled, and is still the law of the case, so far as the dischargeability of this indebtedness is concerned.

If the objecting creditor relies on the judgment of the Circuit Court of Multnomah County, Oregon, then the answer is that that court had no jurisdiction to determine whether or not this debt was or was not a dischargeable one in this proceeding. All that court had before it, and all that it determined or passed upon, was whether or not a new promise had been made by the Bankrupt, which made the discharge granted by the District Court in the former bankruptcy proceedings unavailable to the Bankrupt.

We, therefore, confidently assert that the doctrine of *res judicata* has nothing to do with the issues before this court and cannot be relied upon to support the order appealed from.

## POINT II

We will discuss under this part of the argument, the issues raised by specifications of error 2, 9 and 10.

The court below, in affirming the order of the Referee discharging the bankrupt with qualifications, adopted the opinion of the Referee in all particulars



and held that the bankrupt, by making a new promise to pay the indebtedness of Mildred McDonald (now Mildred Muck), which was scheduled in his first bankruptcy proceeding and from which he obtained a discharge in that proceeding, waived his right to a discharge from this obligation forever. The conclusion so reached by the Referee, in his opinion, is apparently based on the rule adopted in most State Courts that a bankrupt, who has obtained a discharge from an indebtedness by making a new promise to pay such indebtedness, waives his right to plead such discharge as a defense when a subsequent action is brought on this indebtedness.

The Courts, in permitting a recovery on the new promise, have said that the new promise acts as a waiver by the bankrupt of his former discharge.

This waiver is not enforceable in a Bankruptcy Court as such, but always arises and becomes available in actions in State Courts, and it has been said that whether or not such a new promise is enforceable in any case is a matter of the law of the state where such action is brought.

Remington on Bankruptcy, 5th Ed., Sec. 3499.50, Vol. 7, Pg. 756, and cases cited.

Since the State Courts have adopted the doctrine that a bankrupt's discharge may be waived by a subsequent promise, it becomes necessary to determine what is meant by the term "waiver".



There are many definitions of the term waiver, but every such definition embodies certain fundamental necessary elements.

Corpus Juris defines waiver as follows:

“Waiver has been defined as a voluntary and intentional relinquishment or abandonment of a known *existing* legal right, advantage, benefit, claim or privilege which, except for such waiver, the party would have enjoyed.” 67 C. J. Sec. 1, Pg. 289.

In speaking of the necessary elements of a valid waiver, Corpus Juris says:

“In order to constitute a waiver, the right, benefit, or advantage in question must be in existence at the time, although it may be unenforceable. Waiver involves the voluntary relinquishment of some known right which is at the time available; thus, one cannot waive that which is not his as of right at the time of waiver; a person cannot waive a right before he is in a position to assert it. There can be no waiver of a *non-existent* or lost right.” 67 C. J. Sec. 4, Page 299.

Applying the above rule to the facts before this Court in the instant case, it conclusively appears that the Bankrupt, in this case, could not have waived his right to a discharge in the present bankruptcy proceeding when he made a promise, prior to February 7, 1935, to pay the debt of Mildred McDonald which had been scheduled in his first proceedings and from which he had been legally discharged.

Prior to the date of the adjudication in bank-

ruptcy in 1941, being the present bankruptcy proceedings, Bernard G. Shepherd had no right to a discharge in such subsequent proceedings. This right to discharge only arose upon his adjudication in this proceeding which was long after the entry of the judgment in favor of Mildred McDonald (now Mildred Muck), which is scheduled in the present bankruptcy proceeding.

Bearing these principals in mind, just what right did the Bankrupt waive when he made the new promise to the objecting creditor in this case?

Did he waive the right to assert the discharge in bankruptcy granted to him in his first bankruptcy proceedings as a defense to the action which was thereafter immediately instituted against him in the State Court, or did he waive some other right which he then possessed?

Certainly, the only right that he could at that time waive was the right to plead the discharge in bankruptcy, which he then possessed, and had, from the bankruptcy proceedings of 1931.

He certainly did not waive the right to a discharge in this proceeding, because this proceeding did not then exist.

If it is argued that by making the new promise he waived the right to avail himself of the provisions of the Bankruptcy Act in the future, the conclusive answer is that, to so hold, would, in effect, nulify the

express provisions of the Bankruptcy Act which granted to him the absolute right to file subsequent proceedings in bankruptcy which would entitle him to all of the benefits and subject him to all of the responsibilities of the Act.

The Bankruptcy Act provides that one may file a voluntary petition in bankruptcy as often as it may become necessary in the conduct of his affairs. The only prohibition being that he can only obtain a discharge once in six years. When the bankrupt filed his petition in this case, he was required by the provisions of the Act to schedule all his provable debts including that of the objecting creditor. No provision of the act excepts such a claim as this from a discharge and to so hold is to write something into the Act which Congress has not seen fit to do.

The Referee, therefore, is in error when he holds and finds that by making the new promise to the objecting creditor after the entry of the discharge in his prior proceedings, he thereby waived all rights forever to the benefit of the Bankruptcy Act which are guaranteed to him by the solemn enactment of Congress.

### POINT III

#### **Specifications of Error 1.**

The Referee holds, and finds, that the indebtedness which was the basis, and gave rise to the cause of ac-

tion, upon which the judgment of the Circuit Court of Multnomah County, Oregon is based, was the old original debt scheduled in the first bankruptcy proceedings of Bernard G. Shepherd.

The Referee admits that the general rule followed by most of the courts, both State and Federal, is that the cause of action in such a case as this is, in fact, a new obligation and not the old debt.

All of the decisions referred to and cited by the Referee in his opinion admit that the cause of action, in order to be maintainable, must have something more than the original indebtedness existing at the time of the first adjudication in bankruptcy.

It is the old indebtedness, plus the new promise. Both must exist when the action is brought, or a recovery cannot be had. Many of the cases say that the new promise revives the obligation. Most of them, however, state that the new promise operates as a waiver.

The Referee referred to the case of United States National Bank of LaGrande vs. Miller, 118 Oregon, 280; 246 Pacific, 726; and states that this case is an authority for the proposition that this cause of action is on the old indebtedness. An examination of this case shows that the court said that the consideration for such a new promise is the moral obligation of the debtor, using the following language, at page 291:

“The law is well settled that a discharge in bank-

ruptcy, while releasing the bankrupt from liability to pay a debt that is provable in the bankruptcy proceedings, leaves him under a moral obligation sufficient to support a new promise by the debtor to pay the debt, which may be enforced against him."

The Referee holds that authorities, relying upon the doctrine of moral obligation as a consideration to support the new promise to pay the debt, are not sound, citing Williston on Contracts. However, the law in Oregon is to the contrary, and, we believe, should be followed by this court.

In every such case, the pleadings must disclose not only the old indebtedness, but the new promise.

Surely, the cause of action has to be based upon more than the old indebtedness. The element of a new promise is absolutely essential to the maintenance of the cause of action, and the resulting judgment embodies within it both of these elements.

It is, therefore, submitted that the cases which hold a judgment based upon a new promise in such a case as this is an entirely new indebtedness should be followed by this court.

This is the majority rule in the United States:

Matter of Cox, 47 ABR (N.S.) 668, 33 F. Supp. 796.

8 Corpus Juris Secundum, Section 583 (d) Pg. 1577.

Wolffe vs. Eberlein, 74 Ala. 99, 49 Am. Rep. 809.

Matthewson vs. Needham, 81 Kan. 340, 105 Pac. 436, 26 LRA (N.S.) 274.



6 Am. Jur. 535.

Holden vs. Chamberlin, 46 N.D. 353; 179 N.W. 706.

In the last mentioned case, the Supreme Court of North Dakota, in its opinion, point out the reasons why the new promise must, in fact, be a new cause of action, and a new indebtedness, in language which the writer of this brief believes to be unanswerable. The court said:

“The writer, speaking for himself, is of the opinion that a debt or obligation discharged in bankruptcy, while not paid, is wholly extinguished, so far as any future legal liability upon it is concerned; that the debt or obligation no longer exists; that there remains only, after such discharge, the moral obligation to pay the debt; that this moral obligation may be and is, a sufficient consideration for a new contract to pay the debt discharged; that in making such new contract, based upon such moral obligation, the minds of the parties must meet upon all the terms in the same manner and to the same effect as upon any other contract; that is, if the debt for a given amount is discharged in bankruptcy, and the debtor makes a definite promise, after the adjudication, to pay the amount of the debt discharged, stating in such promise certain amounts of the debt to be paid at different times, or promising to pay it all at a certain time, that before a new contract is actually made, which is binding upon both parties, such terms contained in the promise must be accepted by the creditor, and thus constitutes a new contract for the amount of the debt—in other words a new debt—the moral obligation to pay the debt discharged being a sufficient consideration for the new contract.”



An illuminating case on this subject is the recent case of *Matter of Cox*, 47 ABR (N.S.) 668. (U.S. Dis. Ct. W.D.K. July 9, 1940).

In this case Cox, the bankrupt, was adjudicated as such on the 26th day of February, 1937. He made timely application for a discharge which had not been granted at the time the proceedings discussed in the case were had.

Among the debts listed in his schedule was one in favor of the Personal Finance Company. After his adjudication, the Personal Finance Company filed a suit in the State Court in which it alleged, among other things, that the bankrupt made a new promise to pay the debt involved in the suit after his adjudication in this bankruptcy. A judgment was entered against Cox by default.

The Personal Finance Company then proceeded to enforce this judgment in the State Court and the bankrupt petitioned the Bankruptcy Court for a stay.

The bankrupt contended that the Bankruptcy Court had jurisdiction to grant the stay because the claim upon which the judgment was entered in the State Court was dischargeable in his then pending bankruptcy proceedings and that such judgment was, in fact, void. He also contended that no action could be brought upon a new promise until after the question of his discharge had been determined.

The Personal Finance Company contended that this action in the State Court was upon a new promise, made after adjudication, which created an entirely new and separate valid obligation.

District Judge Miller reviewed a large number of decisions on this question, and *held* that the new promise, made after an adjudication even before a discharge was granted, created an entirely new, separate and valid obligation, and that this obligation, having arisen subsequent to the adjudication was like any new debt, unaffected by the prior bankruptcy proceedings. The Court said, on page 673:

“The authorities throughout the country are in conflict on this issue with the weight in favor of the view that the action lies upon the new promise. See 3 R.C.L., Bankruptcy, Sec. 147; 8 Corpus Juris Secundum, Bankruptcy, Sec. 583, sub-division (d).

“Since the action in the state court was upon a promise made after the adjudication in bankruptcy which created a new obligation as of that time, it is not an action on a claim provable or dischargeable in bankruptcy, and accordingly the bankruptcy court has no jurisdiction to interfere with the enforcement of that judgment. Obligations coming into existence after the filing of the petition in bankruptcy, although before the granting of the discharge, are not affected by the discharge subsequently granted which relates back to the filing of the petition.”

This is the most recent case that we have been able to find on this particular subject, and since the court in that case states unequivocally that the weight of

authority is that a new promise gives rise to a new and distinct obligation, we feel safe in saying that that should be the rule in this jurisdiction, and in this court.

Clearly, therefore, if the promise made by the bankrupt subsequent to his adjudication in his bankruptcy proceeding in 1931 created a new and distinct obligation from that scheduled in 1931 it should stand in the same position as any new debt incurred by the Bankrupt subsequent to his adjudication in 1931 and as such is dischargeable in his present proceedings.

Finally, we call the court's attention to the case, *Bluthenthal vs. Jones*, 208 U. S. 64; 52 L. Ed. 390.

In this case, the Supreme Court of the United States held that in order for a creditor whose debt had been scheduled in a first bankruptcy proceeding in which a discharge was denied to keep such debt from being discharged in a second bankruptcy where it was scheduled, that such creditor must interpose objections to the second discharge in the Bankruptcy Court, and failing so to do could not thereafter plead that the discharge in the second proceedings was not binding on such debt.

The facts discussed by the Court were these:

Jones, a bankrupt, obtained a discharge in a bankruptcy proceedings, begun by him in the District Court of the United States in Florida on August 3, 1903, his discharge having been entered on November

7, 1903. The debt involved was one provable in that bankruptcy proceeding, and would be barred by the discharge in that proceeding were it not that Jones, in a prior proceeding in bankruptcy, had scheduled the same debt and the same creditor, Bluthenthal & Bickart, had objected to his discharge in this first proceeding and his discharge had been denied.

In the second proceeding in which the claim of *Bluthenthal & Bickart* was listed, they did not, as creditors, either prove their claim or enter any objections to the bankrupt's discharge.

After his discharge in the second bankruptcy proceeding, Bluthenthal & Bickart started a proceeding in the State of Florida to enforce their judgment. The Bankrupt pleaded his second discharge and Bluthenthal & Bickart, the creditors, set up the fact that this second discharge did not constitute a bar to the enforcement of their judgment because of the fact that the bankrupt had been denied a discharge in the first bankruptcy proceeding in which their claim had also been listed.

The Supreme Court of the United States *held* that the second discharge in bankruptcy was *res judicata* and binding on all Courts, and that if the creditor wished to prevent the discharge of its claim in the second proceeding, it should have set up that matter in the Bankruptcy Court in the proceeding which led up to and resulted in the second discharge. Having failed to do this, the Bankruptcy Court in the second

proceeding had an exclusive jurisdiction to determine the question of discharge in that proceeding. Its grant of a discharge was *res judicata* in all Courts.

The Supreme Court pointed out that the State Court had no jurisdiction to examine into the question of dischargeability or non-dischargeability of this claim by reason of the denial of the bankrupt's first discharge because that court was bound by the later adjudication which granted a discharge in the second proceeding.

The Supreme Court, in passing on the question, said, Pg. 392:

"Section 1 of the bankruptcy act defines a discharge as 'the release of a bankrupt from all of debts which are provable in bankruptcy, except such as are excepted by this Act.'

"Section 14 of the amended act, which was applicable to the second proceedings, provides that after due hearing the court *shall discharge* the bankrupt, unless he has committed one of the six acts specified in that section. Section 17 of the amended act provides that a discharge in bankruptcy shall release a bankrupt from all of his provable debts, with four specified exceptions, which do not cover this case. The discharge appears to have been regularly granted, and, as the debt due to Bluthenthal & Bickart is not one of the debts which, by the terms of the statute, are excepted from its operation, on the face of the statute the bankrupt was discharged from the debt due to them. There is no reason shown in this record why the discharge did not have the effect which it purported to have. Undoubtedly, as in all other judicial proceedings, an adjudication refusing a



discharge in bankruptcy finally determines, for all time and in all courts, as between those parties or privies to it, the facts upon which the refusal was based. But courts are not bound to search the records of other courts and give effect to their judgments. If there has been a conclusive adjudication of a subject in some other court, it is the duty of him who relies upon it to plead it or in some manner bring it to the attention of the court in which it is sought to be enforced. Plaintiffs in error failed to do this. When an application was made by the bankrupt in the district court for the southern district of Florida, the judge of that court was, by the terms of the statute, bound to grant it, unless upon investigation it appeared that the bankrupt had committed one of the six offenses which are specified in § 14 of the bankruptcy act, as amended. An objecting creditor might have proved upon that application that the bankrupt had committed one of the acts which barred his discharge, either by the production of evidence, or by showing that in a previous bankruptcy proceeding it had been conclusively adjudicated, as between him and the bankrupt, that the bankrupt had committed one of such offenses. If that adjudication had been proved, it would have taken the place of other evidence and have been final upon the parties to it. But nothing of this kind took place. Bluthenthal & Bickart intentionally remained away from the court and allowed the discharge to be granted without objection.

*"Since the debt due to the plaintiffs in error was a debt provable in the proceedings before the District court in Florida, and was not one of the debts exempted by the statute from the operation of the discharge, it was barred by that discharge."*  
(Italics ours)

Whether the cause of action upon which the judgment of Mildred McDonald, the objecting creditor,



which ripened into a judgment in the Circuit Court of Multnomah County, Oregon, and which was scheduled in these proceedings, was the old indebtedness scheduled in the original bankruptcy proceedings in 1931 or is, as we contend, an entirely new obligation, does not, in our opinion, effect the question now to be decided.

Bernard G. Shepherd is entitled, as a matter of law, and a matter of right, to a discharge in these proceedings from this judgment in either case.

The doctrine of *res judicata*, relied upon by the Referee in his opinion, has no application to the facts in this record.

The doctrine of waiver cannot apply without denying and refusing to the Bankrupt the benefits of the Bankruptcy Act enacted by the Congress of the United States.

The Bankruptcy Act expressly enjoins upon this court the absolute duty to grant a discharge to this Bankrupt unless it clearly appears that he has been guilty of some of the acts prohibited in subdivision (c) of Section 14 of the Bankruptcy Act.

The record in this case shows as follows:

1. The Bankrupt herein filed his voluntary petition in these proceedings, as he had a right to do, under the provisions of the Bankruptcy Act.

2. The Bankrupt scheduled the judgment of Mil-

dred McDonald, the objecting creditor, in these proceedings, as he was required to do by the Bankruptcy Act.

3. The Bankrupt paid all of the costs and expenses of this proceeding.

4. The judgment of Mildred McDonald was a provable debt and was proven in these proceedings.

5. The Bankrupt has obeyed all of the orders of this court in these proceedings.

6. No facts showing a violation of any of the prohibited acts set forth in subdivision (c) of Section 14 of the Act are shown in the record or are relied on by the objecting creditor.

The above facts show conclusively that an unconditional discharge should have been granted in this case to the Bankrupt.

To ask this court to deny the Bankrupt a discharge in these proceedings against the indebtedness due Mildred Muck, the objecting creditor, is to ask this court to wholly disregard the express provisions of the Bankruptcy Act; is to ask this court to disregard the plain and emphatic directions of Congress as embodied in the Bankruptcy Act.

For this court to disregard the act, and to find some theoretical, impracticable, unsound rule of construction upon which to base an order denying a discharge in this case, would be to make this court a

legislative agency, and not a judicial one.

A holding of this court that the Bankrupt in this case is not entitled to a discharge from the judgment of Mildred Muck would result in adding to the provisions of the Bankruptcy Act a requirement that an indebtedness upon which a discharge had once been granted, and later revived by a new promise, constitutes a new ground for denying a discharge and, in effect, adding a new ground for objection to a discharge which is not contained in the Act.

Had Congress intended any such result, this ground would certainly have been included in the Act, itself; not being so included, it is not available as a ground of objection and cannot be enforced as such in a bankruptcy court.

## CONCLUSION

We respectfully submit that the order, from which this appeal is taken, is erroneous and should be overruled, corrected, and an order entered granting to the Bankrupt a full and complete discharge from all indebtedness including the judgment of Mildred Muck.

Respectfully submitted,

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## APPENDIX A-1

## Section 14, Bankruptcy Act, 11 USCA, Sec. 32

## DISCHARGES, WHEN GRANTED

“a. The adjudication of any person, except a corporation, shall operate as an application for a discharge: *Provided*, That the bankrupt may, before the hearing on such application, waive by writing, filed with the court, his right to a discharge. A corporation may, within six months after its adjudication, file an application for a discharge in the court in which the proceedings are pending.

b. After the bankrupt shall have been examined, either at the first meeting of creditors or at a meeting specially fixed for that purpose,, concerning his acts, conduct and property, the court shall make an order fixing a time for the filing of objections to the bankrupt's discharge, notice of which order shall be given to all parties in interest as provided in Sec. 58 (94) of this Act. (Title). Upon the expiration of the time fixed in such order or of any extension of such times granted by the court, the court *shall discharge the bankrupt* if no objection has been filed; otherwise, the court shall hear such proofs and pleas as may be made in opposition to the discharge, by the trustee, creditors, the United States attorney, or such other attorney as the Attorney General may designate, at such time as will give the bankrupt and the objecting parties a reasonable opportunity to be fully heard.

c. *The Court shall grant the discharge unless satisfied that the bankrupt has (1) committed an offense punishable by imprisonment as provided under this Act (Title); or (2) destroyed, mutilated, falsified, concealed, or failed to keep or preserve books of account or records, from which his financial condition and business transactions might be ascertained, unless the court deems such acts or failure to have been*

justified under all the circumstances of the case; or (3) obtained money or property on credit, or obtained an extension or renewal of credit, by making or publishing or causing to be made or published in any manner whatsoever, a materially false statement in writing respecting his financial condition; or (4) at any time subsequent to the first day of the twelve months immediately preceding the filing of the petition in bankruptcy, transferred, removed, destroyed, or concealed, or permitted to be removed, destroyed, or concealed, any of his property, with intent to hinder, delay, or defraud his creditors; or (5) has within six years prior to bankruptcy been granted a discharge, or had a composition or an arrangement by way of composition or a wage earner's plan by way of composition confirmed under this Act (Title); or (6) in the course of a proceeding under this Act (Title) refused to obey any lawful order of, or to answer any material question approved by, the court; or (7) has failed to explain satisfactorily any losses of assets or deficiency of assets to meet his liabilities: *Provided*, That if, upon the hearing of an objection to a discharge, the objector shall show to the satisfaction of the court that there are reasonable grounds for believing that the bankrupt has committed any of the acts which, under this subdivision (c), would prevent his discharge in bankruptcy, then the burden of proving that he has not committed any of such acts shall be upon the bankrupt \* \* \* \* \* ." (Italics ours)



## Section 17, Bankruptcy Act, 11 USCA, Sec. 35

## DEBTS NOT EFFECTED BY A DISCHARGE

“a. A discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as (1) are due as a tax levied by the United States, or any State, county, district, or municipality; (2) are liabilities for obtaining money or property by false pretenses or false representations, or for willful and malicious injuries to the person or property of another, or for alimony due to or to become due, or for maintenance or support of wife or child, or for seduction of an unmarried female, or for breach of promise of marriage accompanied by seduction, or for criminal conversation; (3) have not been duly scheduled in time for proof and allowance, with the name of the creditor, if known to the bankrupt, unless such creditor had notice or actual knowledge of the proceedings in bankruptcy; or (4) were created by his fraud, embezzlement, misappropriation or defalcation while acting as an officer or in any fiduciary capacity; or (5) are for wages which have been earned within three months before the date of commencement of the proceedings in bankruptcy due to workmen, servants, clerks, or traveling or city salesmen, on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; or (6) are due for moneys of any employee received or retained by his employer to secure the faithful performance by such employee of the terms of a contract of employment.”



No. 11140

In the United States  
Circuit Court of Appeals  
For the Ninth Circuit

BERNARD G. SHEPHERD, *Appellant*,

vs.

MILDRED McDONALD, now  
MILDRED MUCK, *Appellee*.

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Appellee's Brief

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Upon Appeal from the District Court of the United States  
for the District of Oregon

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No. 11140

**In the United States  
Circuit Court of Appeals  
For the Ninth Circuit**

---

BERNARD G. SHEPHERD, *Appellant*,

vs.

MILDRED McDONALD, now  
MILDRED MUCK, *Appellee*.

---

**Appellee's Brief**

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**SUPPLEMENTAL STATEMENT OF CASE**

The facts in the present cause, as set out in the statement of the case appearing in the Appellant's brief (page 2) are substantially correct. However, this statement fails to clearly point out the material and uncontroverted finding of the referee (Tr. 21, 28) that the debt of the objecting creditor, Mildred Muck (appellee) is the same obligation from which the bankrupt secured a discharge in his previous bankruptcy proceeding.

## THE QUESTION ON APPEAL

**Does the Waiver of a Discharge Become a Bar to a Further Discharge of the Same Debts in a Subsequent Proceeding of the Same Bankrupt?**

### POINTS AND AUTHORITIES

#### I.

The bankruptcy court may upon motion of proper party or on its own motion, qualify the discharge of the bankrupt to exempt certain debts not dischargeable in the proceeding.

*Volume 1, Collier on Bankruptcy*, 14th Edition, 1381, 1382, Paragraphs 14.62, 14.63.

*Volume 7, Remington on Bankruptcy*, 696, Section 3441.

*Section 17, Bankruptcy Act*, (U.S.C.A., Title II, Chapter 3, Sec. 35)

*Freshman v. Atkins*, 269 U.S. 121; 70 L. ed. 193; 46 S. Ct. 41.

*Blumenthal v. Jones*, 208 U.S. 64; 52 L. ed. 390.

*In Re Finkelstein*, CCH Bankruptcy Law Service, Par. 55479.

*Matter of Summer*, 107 F. (2d) 396; 41 A.B.R. (N.S.) 246.

*In Re Tucker*, 49 F. Supp. 239; 53 A.B.R. (N.S.) 106.

*In Re Zitzman*, 46 F. Supp. 314; 50 A.B.R. (N.S.) 724.

*Matter of Early*, 34 F. Supp. 774; 43 A.B.R. (N.S.) 518.

*Hisey v. Lewis-Gale Hospital*, 27 F. Supp. 20; 40 A.B.R. (N.S.) 206.

## II.

The waiver of a discharge secured in a bankruptcy proceeding is a bar to a discharge of the same debt in a subsequent proceeding by the same bankrupt.

*Volume 7, Remington on Bankruptcy*, 419, Sections 3184, 3185.

*Volume 7, Remington on Bankruptcy*, 715, Section 3457.50.

*Volume 7, Remington on Bankruptcy*, 849, Section 3586.

*Volume 7, Remington on Bankruptcy*, 1944 Supp. 40, 41, 42.

*Volume 1, Collier on Bankruptcy*, 14th Edition, 1657, Par. 17.27.

*67 Corpus Juris*, 289, Section 1.

*Article 1, Section 8, Constitution of the United States.*

*Section 14c (5) Bankruptcy Act*, (U.S.C.A. Title 11, Chapter 3, Sec. 32)

*Freshman v. Atkins*, 269 U.S. 121, 46 S. Ct. 41, 70 L. ed. 193.

*Matter of Summer*, 107 F. (2d) 396; 41 A.B.R. (N.S.) 246.

*Perlman v. 322 West 72nd Street Co.*, 127 F. (2d) 716; 49 A.B.R. (N.S.) 212.

*Shopnick v. Tokatyan*, 128 F. (2d) 521.

- Colwell v. Epstein*, 142 F. (2d) 138; 56 A.B.R. (N.S.) 97; 156 A.L.R. 836.
- In Re Brown*, 35 F. Supp. 619; 47 A.B.R. (N.S.) 539.
- Kuntz v. Young*, 131 F. 719; 12 A.B.R. 505.
- In Re Loughran*, 218 F. 619; 33 A.B.R. 350.
- Matter of Schwartz*, 248 F. 841; 41 A.B.R. 246.
- Armstrong v. Norris*, 247 F. 253; 40 A.B.R. 735.
- In Re Zeiler*, 18 F. Supp. 539; 43 A.B.R. 627.
- In Re Fiegenbaum*, 121 F. 69; 9 A.B.R. 595.
- In Re Vardell*, 28 A.B.R. (N.S.) 697.
- In Re Bybee*, 124 F. 1011.
- Matter of Baker*, 275 F. 511; 47 A.B.R. 255.
- Matter of Dierck*, 37 A.B.R. (N.S.) 198.
- Prudential Loan and Finance Company v. Roberts*, 52 F. (2d) 918.

### III.

The debt of Mildred Muck, objecting creditor, (appellee), is the same obligation scheduled and discharged in bankrupt's first proceeding.

- Volume 7, Remington on Bankruptcy*, 420 Section 3184.
- Volume 7, Remington on Bankruptcy*, 703, Section 3448.
- Volume 8, Remington on Bankruptcy*, 32, Section 3718.
- Volume 1, Collier on Bankruptcy*, 14th Edition, 1385, Par. 14.67.
- 8 Corpus Juris Secundum*, 1577, Section 583d.
- General Order in Bankruptcy XLVII.*



*Colwell v. Epstein*, 142 F. (2d) 138; 156 A.L.R. 836.

*In Re Kuffler*, 158 F. 1021; 22 A.B.R. 289.

*Matter of Summer*, 107 F. (2d) 396; 41 A.B.R. (N.S.) 246.

*In Re Schnabel*, 166 F. 383; 23 A.B.R. 22.

*Matter of Cox*, 33 F. Supp. 796; 47 A.B.R. (N.S.) 668.

*Tubbs v. McCabe*, 165 Atl. 336.

*United States National Bank of LaGrande v. Miller*,  
118 Or. 280; 245 Pac. 726.

*Holden v. Chamberlin*, 46 N. D. 353; 179 N.W. 706.

*Blumenthal v. Jones*, 208 U.S. 64; 52 L. ed. 390.

## ARGUMENT

### I.

Appellant has contended with some earnestness, that the bankruptcy court has no power to determine the effect of a discharge or to pass upon the question as to whether a particular debt has been discharged. Such argument seems to be untenable in the light of many authorities, which hold that the bankruptcy court has the power to qualify the discharge of the bankrupt upon its own motion, or upon motion of one of the parties to exempt therefrom debts not dischargeable in the proceedings. This rule has been summarized in *Volume 7, Remington on Bankruptcy*, 696, Section 3441, where it is stated: (*italics ours*)

“Nevertheless, where it is not the effect of a discharge on a particular debt that is involved, but rather the right itself to a discharge, and where such right exists as to some creditors and not as to others, as in cases of former denial of discharge, *the court undoubtedly may give effect to the res judicata by excepting debts provable under the former bankruptcy.*”

Many authorities are cited in this text to support the statement, and particular reference is made to *Freshman v. Atkins*, 269 U.S. 121, 123, 46 S. Ct. 41, 70 L. Ed. 193, 6 A.B.R. (N.S.) 744; *Hisey v. Lewis-Gale Hospital*, 27 F. Supp. 20; 40 Am. B.R. (N.S.) 206.

See also *Volume 1, Collier on Bankruptcy*, 14th Ed. 1381, 1382, paragraphs 14.62, 14.63.

*In Re Finkelstein* (U. S. D. C. E. D. N. Y., Oct. 15, 1945,) (C. C. H. Bankruptcy Law Service 55479), it has recently been held that a creditor whose debt had been previously listed in a proceeding from which the bankrupt did not secure a discharge was entitled to secure a qualification of an order of a discharge in a second proceeding commenced by the bankrupt more than ten years after the discharge in the second proceeding was granted.

The foregoing rule is further supported by the many authorities that hold that if a creditor having a non-dischargeable debt, does not secure an exemption from

the discharge, he will be bound by the discharge. A statement to this effect is found in *Volume 7, Remington on Bankruptcy*, 697, Section 3441: (Insertion ours)

“Otherwise, (referring to exemption of dischargeable debt from discharge), such debts, being likewise provable under the present bankruptcy, would be discharged by the present discharge, and the former adjudication be defeated.” (Citing *Blumenthal v. Jones*, 208 U.S. 64; 52 L. Ed. 390.)

If the bankruptcy court grants a discharge, and the debt is a provable and dischargeable debt, it is elementary that a state court is bound by the discharge. On the other hand, if the debt is one that is expressly excepted from discharge under Section 17 of the Bankruptcy Act\*, the effect of the discharge upon the debt may be determined by a state court. However, the situation is far different where the debt is not dischargeable because of a substantive rule of law. Such a rule has been well established from the authorities cited in this brief under Point II, where it appears that a bankrupt, who has not secured a discharge either through his failure to apply or a denial thereof, is not entitled to secure a discharge from any of the debts scheduled in such proceeding in a subsequent proceeding of the same bankrupt.

This rule has become established notwithstanding the

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\* See Appendix.

nondischargeability of certain debts under Section 17 of the Bankruptcy Act\*, and accordingly creates an exemption from the operation of a discharge without legislative enactment but based solely upon judicial determination. The authorities cited heretofore clearly disclose that a creditor entitled to such an exemption must, in order to preserve the exemption, secure a qualified order of discharge in the subsequent proceeding of the bankrupt. See *Blumenthal v. Jones, supra*.

It follows therefore that the referee and the district court in the instant matter were clearly within their power in entering a qualified order of discharge, exempting the debt of the objecting creditor, Mildred Muck, (appellee).

## ARGUMENT

### II.

The referee and the district court have found that the debt of the objecting creditor herein, was discharged in the bankrupt's prior proceeding, but that the bankrupt expressly waived the discharge and agreed to pay the debt irrespective of the discharge, and that as a consequence the debt is exempt from the discharge in the second proceeding.

As has been stated by the referee in his opinion, and by the appellant, this is a matter of original impression.

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\* See Appendix.

No direct authority has been found to sustain or controvert the determination made herein.

It has become well established that the denial of a discharge or the failure to apply therefor in an earlier proceeding where formal application was necessary, is a bar to a discharge of all debts provable in such proceeding in any subsequent proceeding of the same bankrupt. *Volume 7, Remington on Bankruptcy*, 419, Section 3184, 3185. See 1944 Supp. 40, 41, 42; *Volume 1, Collier on Bankruptcy*, 14th Edition, 1657, par. 17.27.

The leading case is *Freshman v. Atkins*, 269 U.S. 121; 46 Sup. Ct. 41; 70 L. ed. 193; 6 A.B.R. (N.S.) 744. Other cases in which this rule has been thoroughly discussed are: *In Re Summer*, (C.C.A. 2d, 1939) 107 F. (2d) 396; 41 A.B.R. (N.S.) 246; *Perlman v. 322 West 72nd Street Company*, (C.C.A. N. Y. 1942) 127 F. (2d) 716; 49 A.B.R. (N.S.) 212; *Shopnick v. Tokatyan*, (C. C.A. 2d, 1942) 128 Fed. (2d) 521; *Colwell v. Epstein*, 142 Fed (2d) 138; 56 A.B.R. (N.S.) 97; 156 A.L.R. 836. *In Re Brown*, 35 F. Supp. 619; 47 A.B.A. (N.S.) 539; *Kuntz v. Young*, 131 F. 719, 12 A.B.R. 505; *In Re Kuffler*, 151 Fed. 12, 12 A.B.R. 16; *In Re Loughran*, 218 Fed. 619; 33 A.B.R. 350.

The foregoing rule has been further extended to provide that an application for discharge made in due time,

but voluntarily withdrawn or abandoned is in legal effect the same as a failure to apply and accordingly a bar to a discharge in a second proceeding of debts provable in the former proceeding. *Volume 7 Remington on Bankruptcy*, 420, Section 3184, Note 17. *Volume 1, Collier on Bankruptcy*, 14th Edition, 1657, par. 17.27. *Freshman v. Atkins*, supra; *Matter of Schwartz* (D. C., Ohio), 248 Fed. 841; 41 A.B.R. 246; *Armstrong v. Norris*. (C.C.A. 8th) 247 Fed. 253; 40 A.B.R. 735; *In Re Zeiler*, (D. C. N. Y.) 18 Fed. Supp. 539; 43 A.B.R. 627.

All pertinent cases on both of the foregoing well established rules, have been collected in an annotation appearing in 156 A.L.R. 839, following the case of *Colwell v. Epstein*. These rules have not been altered by the 1938 amendments to the Bankruptcy Act, wherein it is provided that the application for discharge is automatic upon the bankrupt's adjudication. *Perlman vs. 322 West 72nd Street Co. Inc.*, 127 F. (2d) 716; 49 A.B.R. (N.S.) 212. *In Re Brown*, 35 F. Supp. 619; 47 A.B.R. (N.S.) 539.

In the present instance, the bankrupt secured a discharge of the debt of the objecting creditor in the first proceeding. He voluntarily and expressly waived the discharge, which is in effect no different than voluntarily withdrawing an application made in his prior proceeding, and accordingly is entitled to the same legal effect. The



failure to apply for a discharge when the bankrupt is entitled to it, or the voluntary withdrawal of the application, constitutes a waiver of that right within the definition of waiver that is cited by appellant in his brief at page 37. "Waiver has been defined as a voluntary and intentional relinquishment or abandonment of a non-existing legal right, advantage, benefit, claim or privilege which, except for such waiver, the party would have enjoyed." 67 *Corpus Juris*, 289, Sec. 1.

The authorities that have been cited herein and which have established the rule that a denial or abandonment of a discharge in an earlier proceeding is a bar to a discharge in a second proceeding of debts provable in the former proceeding so hold, because:

(1) To grant a discharge in the second proceeding from debts provable in the earlier proceeding would enable the bankrupt to evade the statutory limitation and place within his control the time when he should act. This would interfere with the speedy administration of the bankrupt's estate and would be contrary to the spirit and purpose of the statute.

(2) The failure to secure a discharge is in effect a judgment by default where no application has been made, or if application has been made, then it has the effect and force of an ordinary judgment. Such a judgment,

it has been held, is conclusively *res adjudicata* between the bankrupt and the creditors whose debts were provable in the prior proceeding. The issues in a subsequent proceeding of the bankrupt in which he applies for a discharge with any or all of the same debts scheduled are identical.

Some of the authorities cited in support of the foregoing rule, point out that the only object of a bankruptcy proceeding in a no asset case is to secure a discharge, and if the bankrupt fails to prosecute an application successfully, or voluntarily waives his right to a discharge, he should be barred from securing a discharge in another proceeding of the debts that were provable in the first proceeding. Such a case, it has been held, is *tantamount to an abuse of process of the court*. *In Re Fiegenbaum*, 121 Fed. 69, 9 A.B.R. 595. *Freshman v. Atkins*, 269 U.S. 121, 123, 46 S. Ct. 41, 70 L. Ed. 193; 6 A.B.R. (N.S.) 744. *In Re Vardell*, 28 A.B.R. (N.S.) 697. *Perlman v. 322 West 72nd Street Co., Inc.*, 127 F. (2d) 716; 49 A.B.R. (N.S.) 212.

We fail to see the pertinence of *In Re Bybee*, 124 F. 1011 (D.C.N.D. Cal. 1903), cited by appellant in his brief at page 27, which holds that a denial of a discharge upon a particular debt in a state court insolvency proceeding is not *res adjudicata*, and binding upon the bank-

ruptcy court where scheduled in a subsequent proceeding by the bankrupt. This authority is contrary to the legion of authorities we have cited herein, establishing the general rule that a denial of a discharge in a bankruptcy proceeding is a bar to securing a discharge in a subsequent proceeding by the same bankrupt from provable debts scheduled in the prior bankruptcy proceeding. To permit the state court insolvency proceeding as in the cited case to effect a bankruptcy discharge would be contrary to the spirit and intent of *Article I, Section 8 of the Constitution of the United States\**, granting to Congress exclusive power to establish uniform laws on the subject of bankruptcy throughout the United States.

*The Matter of Charles S. Baker*, 275 Fed. 511, 47 A.B.R. 255 (D. C. S. D. N. Y. 1921), cited and quoted by appellant in his brief at page 28, is not applicable to the facts at hand. This authority has been cited to sustain the contention that a discharge, or the failure to secure a discharge, is not res adjudicata of the rights of the creditors of the bankrupt. Quoting from this case, as found in appellant's brief, (28) (Italics ours)

“Failure to schedule and consequent failure to discharge a particular debt does not operate to adjudicate that the debt is not dischargeable. There is no res adjudicata doctrine, because nothing had been adjudicated so far as affects an unscheduled debt. If a

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\* See Appendix.

discharge is refused then, of course, that refusal is *res adjudicata*, but, such is not this case. Cases cited by the attorney for the creditor are those where either (1) a discharge was previously refused or (2) where a previous petition in bankruptcy is still pending. Of course, where there is a refusal to discharge, the adjudication necessarily is that for the same reason justified by the statute the bankrupt cannot obtain a discharge of any of his debts.

*"Where there is a previous proceeding pending, obviously the court will not entertain a second proceeding, so far, in any event, as affects debts existent at the time of filing the petition in the first proceeding. The case at bar, however, is different. Here the bankrupt did no act to bar his previous discharge and the effect of failure to schedule was merely to let the debt remain alive. When, therefore the bankrupt after six years seeks a discharge upon a new petition, the act contemplates that he may be discharged of any then existing debts."*

In the foregoing case the debt was not scheduled in the first proceeding, and was thereafter scheduled in a second proceeding by the bankrupt. There can be no question that the failure to secure a discharge from a debt not scheduled (if the creditor had no notice of the bankruptcy) is not *res adjudicata*, and that such an unscheduled debt may be discharged in a subsequent proceeding. See *Volume 7, Remington on Bankruptcy*, 715 Section 3457.50, and page 849, Section 3586.

However, in the instant case, there is no problem of an unscheduled debt in the prior proceeding. The con-

tention is advanced by appellee that the discharge of the debt having been expressly waived, it is no different than a failure to apply for a discharge or a voluntary withdrawal and abandonment of an application for a discharge which is a bar according to the authorities cited herein to a discharge in a subsequent proceeding of all provable debts in the prior proceeding. This rule has been cited with approval in the foregoing opinion.

For the reasons above stated, the case of *Matter of Dierck*, 37 A.B.R. (N.S.) 198, (U.S.D.C. S.D.N.Y., Apr. 1938), cited by appellant in his brief at page 30, is likewise inapplicable.

The facts of *Prudential Loan and Finance Company v. Roberts*, 52 Fed. (2d) 918 (C.C.A. 5th Cir. Oct. 1931), appearing in appellant's brief at page 31, are substantially different than the present matter. In the cited case the bankrupt was discharged in the first proceeding. Subsequently he contracted a new note obligation in favor of the same creditor. He filed a second petition in which he was unable to secure a discharge because it was filed less than six years since the discharge in the first proceeding was granted. (Section 14c (5) Bankruptcy Act,\* U. S. C. A. Title XI, Chapter 3, Sec. 32.) The bankrupt filed a third petition from which he secured a discharge of the note

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\* See Appendix.



obligation, which as has been stated, was executed subsequent to the first discharge, but which was scheduled in the second proceeding in which the bankrupt was unable to secure a discharge. The creditor contended that the debt having been scheduled in the second proceeding, from which no discharge could be obtained because of the express provisions of the Bankruptcy Act, that the debt was not dischargeable in the third proceeding.

The foregoing authority is an exception that the 5th Circuit has adopted to the rule that a denial or failure to apply for a discharge in a prior proceeding is a bar to a discharge of debts provable therein in a subsequent proceeding by the same bankrupt. This case has not been followed in other circuits and as a matter of fact has been expressly overruled by the recent case of *Shopnick v. Tokatyan* (C.C.A. 2d 1942), 128 F. (2d) 521, where the court held as follows:

“Even without that provision we believe that the principle of *res adjudicata* should lead to the same conclusion. Denial of a discharge from provable debts or failure to apply for it within the statutory period, bars an application in a subsequent proceeding for discharge from the same debts. *Freshman v. Atkins*, 269 U.S. 121, 46 S. Ct. 41, 70 L. ed. 193; *Perlman vs. 322 West 72nd Street Co.*, 127 F. (2d) 716; 49 A.B.R. (N.S.) 212; *In Re Summer*, 107 F. (2d) 396; 41 A.B.R. (N.S.) 246; *In Re Schwartz*, (CCA 2nd) 89 F (2d) 192.

“We think this equally true whether the denial of the discharge was because of a previous discharge



within six years as in the case at bar, or on some other ground specified in section 14. In *re McCausland* (D C S D Cal) 9 F. Supp. 129; appeal dismissed (9 Cir) 79 F. (2d) 1001; *Prudential Loan & Finance Co. v. Robarts* (5 Cir) 52 F. (2d) 918; is to the contrary and Prof. Moore thinks it preferable to the McCausland decision. 1 Collier on Bankruptcy 14th Ed. page 1372, c/f 45, Harvard Law Review 1910. We respectfully disagree and believe that the appellant's (creditor) claim was not dischargeable in the third bankruptcy; consequently it was wrong to stay prosecution of it in the state court. In *Re McCausland*, *supra*."

In *Shopnick v. Tokatyan*, *supra*, the Circuit Court of Appeals for the 2nd Circuit, relied upon the opinion in *Re McCausland*, (D. C. S. D. Cal) 9 F. Supp. 129, (appeal dismissed 9th Cir. 79 F. (2d) 1001), a decision in this circuit and which should be the better rule than that adopted in the case of *Prudential Loan & Finance Company v. Robarts*, *supra*. In the latter case, even conceding the exception to the general rule as determined therein, it is submitted that it is not applicable in the instant matter. Such an exception is based wholly on the contention that in an application for a discharge, commenced by a bankrupt within six years after securing a discharge in a former proceeding, the second proceeding is a futility. This is not the situation in the present matter.

Appellant is apparently not clear in his recognition

of the basis of the referee's order in the present matter. At page 34 of his brief, he contends that if the referee has determined that the debt of the objecting creditor is not dischargeable in the present proceeding because of the doctrine of *res adjudicata*, that the fact that in the first bankruptcy proceeding the debt in question was discharged, establishes that it should be discharged in the present proceeding. This is not the correct interpretation of the referee's opinion and order.

Simply stated, the referee has found that the debt of the objecting creditor being scheduled in the first proceeding and discharged therein, that it possesses all the inherent incidents so far as that proceeding is concerned. Furthermore, that inasmuch as the bankrupt has waived the discharge of the debt, such a waiver is the same as a voluntary withdrawal or abandonment of the bankrupt's application for a discharge in the first proceeding, and in accordance with the well established rule, the fact that the debt was scheduled in the first proceeding and a discharge expressly waived, a bar exists against the same debt being discharged in a subsequent proceeding.

In other words, so far as this particular creditor and the bankrupt is concerned, the dischargeability of the debt having once been before the bankruptcy court for

determination, it is *res adjudicata*. It is conceded that the holding may be different if the debt scheduled in the second or subsequent proceeding is a new debt, but this is not the situation in the existing matter.

The debt as it now exists in the form of a judgment was secured in the Circuit Court of the State of Oregon in a proceeding in which the bankrupt asserted the defense of the first discharge and the creditor made a plea of express waiver of the discharge. All of these matters in controversy in that action are now *res adjudicata*.

The waiver of the discharge in the first bankruptcy proceeding being one of the issues in the action in the state court and having been adjudicated in favor of the objecting creditor, it must be concluded that the judgment in that action was upon the original debt, and not upon a new debt. The referee in his opinion has so found (Tr. 21, 28). A more extensive discussion of whether the debt in the present matter is the same obligation as was scheduled in the first proceeding of the bankrupt is the subject of the argument under Point III of this brief.

It follows that the bankrupt having expressly waived the discharge as it affected the debt of the objecting creditor cannot secure a discharge of the same obligation in any subsequent proceeding.

## ARGUMENT

## III.

The finding of the referee as appears in his opinion, which has been adopted by the district court, and is based upon evidence submitted at a hearing and clearly establishes that: "The objecting creditor's claim is based upon a judgment obtained in an action for the recovery of money owing on certain notes scheduled in the previous bankruptcy, (Tr. 21) \* \* \* "That the debt owing the objecting creditor is the same obligation from which the bankrupt received a discharge in his first bankruptcy." (Tr. 28).

It has been held that the referee's findings of fact are to be accepted by the judge unless clearly erroneous. *Volume 1, Collier on Bankruptcy*, 1385, par. 14.67. This has been similarly stated in *Volume 8, Remington on Bankruptcy*, 32, et seq., Section 3718. The foregoing texts discuss the effect of the following General Order XLVII promulgated by the United States Supreme Court and applicable to bankruptcy proceedings:

"Unless otherwise directed in the order of reference the report of a referee or of a special master shall set forth his findings of fact and conclusions of law, and the judge shall accept his findings of fact unless clearly erroneous. The judge after hearing may adopt the report or may modify it or may reject it in whole or in part or may receive further evidence or may recommit it with instructions."

It is difficult to see how the finding of the referee, as referred to herein, can be considered erroneous. As we have heretofore pointed out, in the action commenced in the Circuit Court of the State of Oregon, a determination was made that the discharge of the original debt was waived, and accordingly the action therein commenced was upon the old obligation and not a new one. The referee in his finding has given proper effect to the determination of the state court action.

Many authorities can be found to give legal effect to the rule that a discharged debt subsequently revived by a new promise does not lose its original incidents, and is considered the old debt, and not a new one, except as in some instances when the express intention of the parties appears to clearly create a new debt by the new promise. To this effect, reference is made to 8 *Corpus Juris Secundum*, 1577, Section 583d (cited by appellant in his brief at page 41)

“The authorities are not in accord on the question of whether the new promise or the old debt forms the basis for recovery against the bankrupt. There are on the one hand those cases which hold that, since the new promise serves merely to revive the original debt, the creditor is required to declare on the original obligation rather than on the new promise, the terms of the old obligation or engagement being the test or measure of the recovery. Other cases, however, take the view that the discharge in bankruptcy extinguishes the original obligation. The new promise

creating a new cause of action which forms the basis of the recovery.

“Apparently recognizing the conflict aforesaid but regarding it as merely one of form, there are cases which hold that the creditor may proceed either on the original debt or on the new promise, and if the old debt be declared on, the new promise may be set up by way of reply.”

The rule enunciated in the foregoing text and adopted by many courts is based on the well established rule summarized in *Volume 7, Remington on Bankruptcy*, 703, Section 3448, as follows: (parenthesis ours)

“Discharge is neither a payment nor an extinguishment of debts; it is simply a bar to their enforcement by legal proceedings.” (Numerous cases are cited in this text in support of this principle, and perhaps the leading case is *Zavelo v. Reeves*, 227 U.S. 625; 57 L. ed. 676; 33 Sup. Ct. 365; 29 A.B.R. 493.)

For a complete discussion of this subject with reference to the particular debt in the present matter, we refer this court to the exhaustive opinion of the learned referee, and more particularly that portion commencing on page 20, Transcript of Record, and continuing through page 27. It is difficult to elaborate upon the reasons and authorities found in the referee's opinion.

In appellant's brief, at page 40, he has urged, in a discussion of the case of *United States National Bank of*



*LaGrande vs. Miller*, 118 Or. 280; 245 Pac. 726, that the rule adopted by the Supreme Court of the State of Oregon is to the effect that a debt discharged in bankruptcy and revived by a new promise is a new debt. The portion of the opinion of the foregoing case quoted by appellant refers only to the rule then in existence to the effect that the moral consideration of the discharged debt is sufficient to support a new promise. As has been pointed out by the referee in his opinion (Tr. 25) cited above, such a rule is not entirely in accord with the more recent trend that the rights of a discharged creditor under such circumstances are not based on a moral consideration.

Furthermore, in the case of *United States National Bank vs. Miller*, *supra*, the court did not limit its holding to the matter quoted in appellant's brief and cited herein, but it held that whether the debt was a new or old one, even after the execution of new notes, *was only a matter of form*. We quote from this case at page 295 of the Oregon Reports: (italics ours)

"We notice there is some respectable authority for the proposition that a debt barred in bankruptcy is not revived by a new promise to pay the same as suggested by the answer; and that an action to enforce payment thereof must be based upon the new promise. *As we have noted in regard to defendant's answer, this is only a matter of form*. See note J, 135 Am. St. Rep. 387. It is stated in 7 C.J. 413, Section 732, as follows:

“‘An action to recover the debt may be based either on the original debt or on the new promise. The pleadings in such an action are subject to the usual rules of construction.’

“The written contract was offered in evidence, among other things, as a defense to plaintiff’s second and third causes of action, which are based upon the new post bankruptcy notes executed during the two years plaintiff was financing defendant in his farming operations. All of the seven notes and renewals thereof given plaintiff by defendant during 1921 and 1922 were fully explained by the cashier of the bank during the trial and counsel for defendant stated at the time that defendant accepted the statement of the bank in regard thereto. So, further comment in regard to such new notes is unnecessary.”

Appellant in his brief at page 41 has cited authorities which he claims is the majority rule for the proposition that a judgment based upon a new promise is an entirely new indebtedness. With the contention that that is the majority rule, appellee must disagree. Ample authority may be found to the contrary. *In Volume 7, Remington on Bankruptcy*, 420, Section 3184, Note 16, it is stated:

“And the putting of a debt provable in bankruptcy into judgment, after the expiration of the time within which to apply for a discharge, creates no new debt, so as to entitle the bankrupt to institute a new bankruptcy proceedings.”

A similar statement of the rule is found in the anno-

tation following the case of *Colwell v. Epstein*, reported in 156 A.L.R. 836, 838, where the editor in support thereof, cites the following authorities:

*Re Kuffler* (1909; CCA 2d), 158 F. 1021, 22 Am. Bankr Rep 289 (writ of certiorari denied in (1909) 214 US 520, 53 L ed 1066, 29 S Ct 701);

*Re Summer* (1939 CCA 2d) 107 F (2d) 396, 41 Am. Bankr Rep (NS) 246 (writ of certiorari denied in (1940) 309 US 680, 84 L ed 1024, 60 S Ct 718);

*Re Schnabel* (1909; DC) 166 F 383, 23 Am Bankr Rep. 22.

An analysis of *Holden v. Chamberlin*, 46 N.D. 353; 179 N.W. 706, cited in appellant's brief at page 42, discloses that the Supreme Court of North Dakota has held: "That an obligation discharged in bankruptcy is wholly extinguished." This is directly opposite and opposed to the opinion of the United States Supreme Court in the *Case of Zavello v. Reeves*, supra, and the many other cases supporting the proposition that a discharge is neither a payment nor extinguishment of debts, but is simply a bar to their enforcement by legal proceedings, as appears in Section 3448 of *Volume 7, Remington on Bankruptcy*, 703, heretofore cited.

Reference is made by the appellant on page 43 of his brief to support his contention that the debt in the present matter is a new one by quoting from the opinion

in the case of *Matter of Cox*, 33 F. Supp. 796; 47 A.B.R. (N.S.) 668. (U.S.D.C.W.D.K. July 9, 1940). In this case the bankrupt petitioned for an injunction restraining the creditor from further proceedings against him in an action in the Jefferson Circuit Court of Kentucky. This action was commenced by the creditor after the bankrupt's adjudication, but prior to his application for discharge, based upon a new promise that the bankrupt made to the creditor subsequent to the adjudication. The bankrupt permitted a default judgment to be entered against him (no specification in the judgment appearing as to whether the same was secured on a cause of action of the old debt as revived or upon a new debt). A reading of this opinion further discloses that the court construed that a new debt was created. Quoting from page 798, of the Federal Supplement Report:

"If the action in the state court was upon a claim which was dischargeable in bankruptcy, the judgment which was obtained has no more validity than the original claim itself. The debt on which the judgment was rendered is the same old debt that it was before notwithstanding the change in its form from that of a simple contract debt or unliquidated claim by merger into a judgment of a court of record. *Boyington v. Ball*, 121 U.S. 457, 7 S.Ct. 981; 30 L. ed. 985.

"This situation is materially different in legal effect from the case where a judgment is rendered after the discharge in bankruptcy has been granted and the defendant fails to plead his discharge. In such cases the judgment has been held to be valid. *Dimock v. Revere Copper Company*, 117 U.S. 559, 6 S. Ct.

855; 29 L. ed 994, Jackson v. Shaw, 20 Cal. App. 2d 740, 68 P. (2d) 310.

"In the present case it was impossible for debtor to plead his discharge in bankruptcy to the action instituted in the state court because no such discharge had been obtained at the time when the judgment was rendered.

"If the judgment in the state court is upon the new promise rather than upon the old indebtedness, a different situation exists, because the new promise is not a claim provable or dischargeable in bankruptcy. The claim based on the new promise comes into existence after adjudication;"

In the foregoing opinion there was no question of waiver of the discharge involved. The bankrupt did not even have an opportunity to interpose the defense of his discharge inasmuch as the action was commenced while the bankruptcy proceeding was pending. As has been stated, the judgment failed to disclose whether the action was commenced upon the old debt as revived, or upon a new debt. From the court's holding as quoted herein, it appears that it considered the debt an entirely new one. These facts are far different than in the instant matter where the referee, as well as the state court, have found that the debt now existing is the same obligation from which the bankrupt secured a discharge in the first proceeding.

Appellant has next cited and quoted in his brief the



case of *Blumenthal v. Jones*, 208 U.S. 64; 52 L. ed. 390 (appellant's brief 45.)

The holding of this opinion is not germane to the issue as to whether the debt involved herein is the same obligation from which the bankrupt secured a discharge in his first proceeding. In the foregoing case, the Supreme Court of the United States held that in a subsequent proceeding of the same bankrupt in which he scheduled the same debt, which had not been discharged in an earlier proceeding, it was necessary for the creditor to secure a qualified order of discharge in order to exempt his debt from the effect of the second discharge. In the cited case the creditor did not take this action, and the court having no knowledge of the prior denial of the discharge, it was held that the creditor had waived the effect of the denial of the discharge in the first proceeding, and was subject to the full force and effect of the discharge in the second proceeding.

These facts are obviously far different than the facts in the present matter. As has been contended in the argument under Point I of this brief, where the foregoing case was cited, it is authority for the proposition that a bankruptcy court may qualify an order of discharge to exempt therefrom any debts not dischargeable in the proceeding, and that if a creditor does not appear



in the proceeding and does not assert his right to such exemption, he will be bound by the discharge.

In the referee's opinion (Tr. 25), as well as the brief of the appellant (p. 40), the rule is stated that most of the cases which deal with the question as to whether a discharged debt as revived by a new promise is a new or old debt hold that a new promise operates as a waiver.

Particular reference is made in support of the foregoing proposition to *Tubbs v. McCabe* (Del.) 165 Atl. 336, 338, where it was held as follows: (*italics ours*).

"The defendant \* \* \* contends that the old debt furnishes the foundation or consideration for such promise and that the rights of the plaintiffs are necessarily based on such contract \* \* \* True, the new promise may, as a general rule, even be conditional and such a promise, if made, is the measure of the plaintiff's right whether relied on to raise the bar of the statute of limitations, or in a case where a defendant has been adjudicated a bankrupt \* \* \*; but where the statute of limitations is involved it is well settled in this state that the action should be on the old debt and not on the new promise to pay. \* \* \* *This can only be on the ground that the defense of the statute is waived \* \* \*; and the same general principles naturally apply to promises to pay made by a bankrupt.* Restatement of the Law of Contr., vol. 1, section 86; 7 Rem. on Bankr. section 3499. In fact, the old theory that the rights of the plaintiffs in such cases are based on a moral consideration has now been very generally exploded. 1 Willist. on Contr. section 148. It is true that for some reason a specific promise to pay is necessary to remove the bar of the

statute in bankruptcy cases while a promise to pay will be inferred from a mere acknowledgment of a subsisting demand where the statute of limitations is involved \* \* \* but whatever the reason for this difference may be, it does not affect the rule above stated."

It should follow that if the new promise operates as a waiver, and the debt is not extinguished by the discharge, the waiver may be plead in avoidance of the defense of a discharge in an action commenced upon the original obligation. This was the situation in the matter at bar.

## CONCLUSION

It must be concluded, that if, as contended by the objecting creditor (appellee), the discharge in the present proceeding cannot affect her debt, it is essential that she secure a qualified order of discharge exempting her debt from the discharge. The power of the bankruptcy court to enter a qualified order appears to be clear in the light of the authorities that have been cited herein.

The order of the referee and the district court herein qualifying the discharge of the bankrupt to exempt therefrom the debt of the objecting creditor, is amply sustained in fact and in law. The rule has been well

settled, that a denial of a discharge whether upon grounds asserted under the provision of Section 14c, of the Bankruptcy Act, or any other substantive rule of law, is a bar to a discharge of provable debts in the first proceeding in any subsequent proceeding of the same bankrupt. The basis of the rule is the elimination of any circumvention of the time limitation imposed by the statute on the bankrupt in securing his discharge, the doctrine of *res adjudicata* as well as the fact that to permit the further discharge would also be vexatious and an imposition upon the court and its decree. The waiver of the discharge falls within the above rule, inasmuch as it is no different than the actual waiver of the right to the discharge by failing to apply for same in due time, or voluntarily withdrawing or abandoning an application for it. To hold otherwise would permit the bankrupt to make an arrangement with a creditor who might successfully oppose his discharge to refrain from asserting his objections to the bankrupt's discharge. This would be detrimental to all the other creditors and the administration of the spirit and intent of the Bankruptcy Act.

As to the matter of whether the obligation of the objecting creditor is the same debt, as the one from which the bankrupt secured a discharge in the prior proceeding, there should be very little doubt. The finding of the referee, which is uncontroverted, and which has been

adopted by the district court is clear in this particular. In addition thereto, the judgment of the Circuit Court of the State of Oregon clearly discloses that the issues therein involved the old debt and the waiver of the discharge of the bankrupt as it affected it and not a new obligation. Thus, in two proceedings has this matter been fully determined. Furthermore, the law as cited herein, amply justifies the legal conclusion that there has been no new debt created by the waiver of the discharge of the bankrupt in the first proceeding.

It is respectfully submitted that the order of the district court based upon the order of the referee excluding the obligation of the objecting creditor herein from the discharge of the bankrupt is correct and proper and should be affirmed by this court.

Respectfully submitted,

MOE M. TONKON,

W. E. RICHARDSON,

*Attorneys for Appellee.*

## APPENDIX

Article I, Section 8, Constitution of the United States:

“Powers of congress. The congress shall have power \* \* \*

“To establish an uniform rule of naturalization, and uniform laws on the subject of bankruptcies throughout the United States; \* \* \*”

Section 14 (c) Bankruptcy Act (U.S.C.A., Title 11, Chapter 3, Section 32)

“The court shall grant the discharge unless satisfied that the bankrupt has: \* \* \* (5) within six years prior to bankruptcy been granted a discharge, or had a composition or an arrangement by way of composition or a wage earner’s plan by way of composition confirmed under this Act \* \* \*”

Section 17, Bankruptcy Act (U.S.C.A., Title 11, Chapter 3, Section 35).

“Debts Not Affected by a Discharge. a. A discharge in bankruptcy shall release a bankrupt from all of his probable debts, whether allowable in full or in part, except such as (1) are due as a tax levied by the United States, or any State, county, district, or municipality; (2) are liabilities for obtaining money or property by false pretenses or false representations, or for willful and malicious injuries to the person or property of another, or for alimony due or to become due, or for maintenance or support of wife or child, or for seduction of an unmarried female, or for breach of promise of marriage accompanied by seduction, or for criminal conversation; (3) have not

been duly scheduled in time for proof and allowance, with the name of the creditor, if known to the bankrupt, unless such creditor had notice or actual knowledge of the proceeding in bankruptcy; or (4) were created by his fraud, embezzlement, misappropriation or defalcation while acting as an officer or in any fiduciary capacity; or (5) are for wages which have been earned within three months before the date of commencement of the proceedings in bankruptcy due to workmen, servants, clerks, or traveling or city salesmen, on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; or (6) are due for moneys of an employee received or retained by his employer to secure the faithful performance by such employee of the terms of a contract of employment."



No. 11144

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United States  
Circuit Court of Appeals  
For the Ninth Circuit.

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PETER L. YOUNG,

Appellant,

vs.

TERRITORY OF HAWAII,

Appellee.

---

Transcript of Record

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UPON APPEAL FROM THE SUPREME COURT FOR  
THE TERRITORY OF HAWAII

FILED

NOV 30 1945

PAUL P. O'BRIEN,  
CLERK







No. 11144

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United States  
Circuit Court of Appeals  
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UPON APPEAL FROM THE SUPREME COURT FOR  
THE TERRITORY OF HAWAII





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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS  
OF RECORD

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and

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Honolulu, T. H.,  
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W. Z. FAIRBANKS,  
Public Prosecutor,

and

J. E. PARKS,  
Assistant Public Prosecutor,  
Honolulu Hale,  
Honolulu, T. H.,  
Attorneys for Defendant in Error. [1\*]

---

\*Page numbering appearing at foot of page of original certified Transcript of Record.

In the Circuit Court of the First Judicial Circuit,  
Territory of Hawaii

January Term, 1942

Criminal No. 16633

Abortion

THE TERRITORY OF HAWAII

vs.

PETER L. YOUNG and HILDA NOZAWA,  
Defendants.

### INDICTMENT

The Grand Jury of the First Judicial Circuit of the Territory of Hawaii do present that Peter L. Young and Hilda M. Nozawa, at the City and County of Honolulu, Territory of Hawaii, and within the jurisdiction of this Honorable Court on the 8th day of August, 1942, maliciously, wilfully, unlawfully and feloniously, and without lawful justification, did use and employ an instrument and a certain noxious substance, a more particular description of which are to the Grand Jury unknown, by then and there forcing said instrument and said noxious substance into the body and womb of a certain woman, to-wit, one Rose Dolim, she, the said Rose Dolim being then and there pregnant and not quick with child, with intent on the part of them, the said Peter L. Young and Hilda M. Nozawa, then and there and thereby to use the said instrument and noxious substance as aforesaid to produce and pro-

cure the miscarriage of the said Rose Dolim, and that the said use of the said instrument and noxious substance was not for the purpose of saving the life of her, the said Rose Dolim, and did then and there and thereby commit the crime of abortion, contrary to the form of the statute in such case made and provided. [4]

A true bill found this 15th day of October, 1942.

M. E. McKENNEY,

Foreman of the Grand Jury.

CHAS. E. CASSIDY,

Public Prosecutor of the City  
and County of Honolulu.

Indictment presented and filed at 3:44 o'clock P. M., October 15, 1942. O. Sezenevsky, Clerk.

Arraignment—1st Def. Oct. 17, 1942. 2nd Def., Oct. 16, 1942.

Plea—Not guilty (both Def'ts), Oct. 23, 1942.

Copy of the within indictment before arraignment furnished 2 Defendants.

PUBLIC PROSECUTOR,

City and County of Honolulu.

[Endorsed]: Filed Sept. 6, 1945. [3]

[Title of Court and Cause.]

INSTRUCTIONS REQUESTED BY THE  
TERRITORY OF HAWAII

The Territory of Hawaii requests the Court to give to the Jury in the above entitled action, the following instructions numbered from 1 to 10, inclusive.

Dated at Honolulu, T. H., this 19th day of March,  
A.D. 1943.

TERRITORY OF HAWAII.  
By JOHN E. PARKS,  
Assistant Public Prosecutor.

TERRITORY'S INSTRUCTION No. 1

Gentlemen of the Jury, I instruct you that the defendant in this case stands charged in the indictment with the crime of abortion.

You are the exclusive judges of the facts in this case and the credibility of the witnesses but the law you must take from the court as given you in these instructions to be the law notwithstanding any opinion you might have as to what the law is or should be.

Given by Agreement.

A. M. CRISTY,  
Judge. [8]

TERRITORY'S INSTRUCTION No. 2

I further instruct you that abortion is defined in our statutes as follows:

“Whoever maliciously, without lawful justification, administers, or causes or procures to be administered any poison or noxious thing to a woman when with child, in order to produce her miscarriage, or maliciously uses any instru-



ment or other means with like intent, shall, ~~if the woman be then quick with child, be punished . . . and~~ if she be then not quick with child, ~~shall~~ be punished . . .”

Sec. 6232—R. L. of H., 1935.

Given as modified by Agreement.

A. M. CRISTY,

Judge. [9]

### TERRITORY'S INSTRUCTION No. 3

I further instruct you that “malice” is defined in our statutes as follows:

“Malice in respect to the commission of any offense, except in cases where it is otherwise expressly provided or plainly intended, includes not only hatred, ill-will and desire of revenge; but, ~~cruelty of disposition or temper; and~~ also a motive or desire of gain or advantage to the offender or another; or of doing a wrong or injury to any person or persons, or to the public. It also includes the acting with a heedless, reckless disregard or gross negligence of the life or lives, the health or personal safety, or legal rights or privileges of another or others, many or few, known or unknown; also the wilful violation of a legal duty or obligation, and wilful contravention of law.”

Sec. 5302, R. L. of H., 1935.

Given as modied by Agreement.

A. M. CRISTY,

Judge. [10]

## TERRITORY'S INSTRUCTION No. 4

You are instructed that it is no defense under the law to the crime of abortion as charged in the indictment that Rose Dolim solicited, requested or consented to have an abortion performed upon her body even if you so find the fact to be.

Given Over Objection.

A. M. CRISTY,  
Judge. [11]

## TERRITORY'S INSTRUCTION No. 5

The jury is instructed that an actual miscarriage is not necessary under the statutes with which the defendant is charged in this case. The crime is complete if a person maliciously, without lawful justification, administers any poison or noxious thing to a woman, when pregnant, in order to procure her miscarriage, or maliciously uses an instrument on a woman, when pregnant, with intent to procure her miscarriage. It is wholly immaterial whether or not a miscarriage actually results.

Sec. 6232, R. L. of H., 1935. 1 Amer. Jur. 136, Sec. 12.

Given Over Objection.

A. M. CRISTY,  
Judge. [12]

## TERRITORY'S INSTRUCTION No. 6

The court further instructs you that our statute also provides that every one shall be presumed to in-

tend the natural and plainly probable consequences of his acts.

Sec. 5358, R. L. of H., 1935.

Given Over Objection.

A. M. CRISTY,  
Judge. [13]

### TERRITORY'S INSTRUCTION No. 8

The court further instructs you, gentlemen of the jury, that you are the exclusive judges of the credibility of the witnesses, of the weight of the evidence, and of the facts in this case. It is your exclusive right to determine from the appearance of the witnesses on the witness stand, their manner of testifying, their apparent candor or frankness, or lack thereof, which witness or witnesses are more worthy of credit, and to give weight accordingly. In determining the weight to be given the testimony of the witnesses you are authorized to consider their relationship to the parties, if any, their interest, if any, in the result of this case, their temper, feeling or bias, if any has been shown, their demeanor on the witness stand, their means and opportunity of information, and the probability or improbability of the story told by them.

If you find and believe from the evidence that any witness in this case has knowingly and wilfully sworn falsely to any material fact in this trial or that any witness has knowingly and wilfully exaggerated or suppressed any material fact or circumstance in this trial for the purpose of deceiving, mis-

leading or imposing upon you, then you have a right to reject the entire testimony of such witness except insofar as the same is corroborated by other credible evidence or believed by you to be true.

Given by Agreement.

A. M. CRISTY,  
Judge. [14]

### TERRITORY'S INSTRUCTION No. 9

I further instruct you that the burden of proof is upon the Territory and the law presumes the defendant to be innocent, and this presumption continues and attends him at every stage of the case until it has been overcome by evidence which proved him guilty to your satisfaction and beyond a reasonable doubt. And in this connection, I instruct you that the doubt which will entitle the defendant to an acquittal must be a reasonable doubt, not a conjured-up doubt, such a doubt as you might conjure up to acquit a friend, but a doubt that you could give a reason for.

A reasonable doubt is not a slight doubt, not a probable doubt, not a possible doubt, not a conjectural doubt, not an imaginary doubt, not a doubt of the absolute certainty of the guilt of the accused, because everything relating to human affairs and depending upon *mortal* evidence is open to conjectural or imaginary doubt, and because absolute certainty is not required by law. The real question is whether after hearing the evidence and from the evidence you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty

and if you have such belief so formed, it is your duty to convict and if you have not such belief so formed it is your duty to acquit.

Given Over Objection.

A. M. CRISTY,

Judge. [15]

### TERRITORY'S INSTRUCTION No. 10

I further instruct you that in connection with the charge of abortion you may bring in, one of the following verdicts as the facts and circumstances in evidence under the law as given you in these instructions may warrant:

1. Guilty as charged; or
2. Not guilty.

Given by Agreement.

A. M. CRISTY,

Judge. [16]

### TERRITORY'S INSTRUCTION No. 11

You are instructed that the burden is on the Territory to prove beyond a reasonable doubt that the defendant's treatment of Rose Dolim was not for the purpose of saving her life.

Given by Agreement.

A. M. CRISTY,

Judge.

[Endorsed]: Filed March 22, 1943. [17]

[Title of Court and Cause.]

REQUESTED INSTRUCTIONS ON BEHALF  
OF DEFENDANT

Peter L. Young, defendant above named, requests this Honorable Court to give to the jury in the above entitled court and cause the following instructions numbered from 1 to . . . ., inclusive.

Dated: Honolulu, T. H., this 18th day of March, 1943.

PETER L. YOUNG,  
Defendant,  
By J. V. ESPOSITO,  
His Attorney. [19]

INSTRUCTION No. 2

I instruct you that the issue which you are to try is that presented by the indictment, and the defendant's plea of not guilty in this case. For be it remembered that the plea of not guilty puts in issue and requires the prosecution to prove each and every material allegation in the indictment beyond all reasonable doubt.

Given by Agreement.

A. M. CRISTY,  
Judge. [20]

INSTRUCTION No. 3

The indictment in this case is a mere accusation and is not of itself any evidence, not the slightest, of the defendant's guilt, and no juror should per-



mit himself to be to any extent influenced because or on account of the indictment against the defendant. You are instructed that the defendant is presumed by the law to be innocent of the crime charged against him, in each and all its parts, and this presumption shields and protects him throughout each and every stage of the trial until overcome by satisfactory evidence, which convinces you of his guilt as charged beyond all reasonable doubt.

Given by Agreement.

A. M. CRISTY,  
Judge. [21]

#### INSTRUCTION No. 4

Moreover, I instruct you that this presumption of innocence is not a mere form to be disregarded by you at pleasure, but it is an essential, substantial part of the law of the land, and is binding upon you in this case, and it is your duty to give the defendant the full benefit of this presumption and to acquit him unless, as I have already stated, the evidence satisfies you of his guilt beyond all reasonable doubt.

Given by Agreement.

A. M. CRISTY  
Judge. [22]

#### INSTRUCTION No. 6

The burden of proof, as those words are understood in criminal law, is never upon the accused to establish his innocence or to disprove the facts

necessary to establish the crime for which he is indicted. It is on the prosecution from the beginning to the end of the trial and applies to every element necessary to constitute the crime.

Given by Agreement.

A. M. CRISTY

Judge. [23]

#### INSTRUCTION No. 7

Under the law no jury can convict a person charged with crime upon mere suspicion, however strong, or simply because there is a preponderance of all the evidence in the case against him, or simply because there are strong reasons to suspect him guilty. What the law requires before a person can be convicted of crime is not suspicion, not mere probabilities, but proof which excludes all reasonable doubt of his innocence.

Given by Agreement.

A. M. CRISTY

Judge. [24]

#### INSTRUCTION No. 8

I further instruct you, as a matter of law, that one accused and on trial charged with the commission of a crime may testify in his own behalf, or not, as he pleases. You are instructed that when a defendant does testify in his own behalf, then you have no right to disregard his testimony merely because he is accused of crime; that when he does

so testify he at once becomes the same as any other witness, and his credibility is to be tested by, and subjected to, the same tests as are legally applied to any other witness.

7 LRA (N S) 1149

Given by Agreement.

A. M. CRISTY

Judge. [25]

INSTRUCTION No. 12

I instruct you that a duly licensed physician may under our statutes lawfully procure the miscarriage of a woman pregnant with child by any means appropriate and reasonable for that purpose whether directly or indirectly applied, if in doing so, he acts in good faith for the preservation of the life ~~or health~~ of such woman, and if you find from all the evidence that the defendant did act in such good faith to preserve the life ~~or health~~ of Rose Dolim, then you must find the defendant not guilty.

6233.

Given by Agreement.

A. M. CRISTY

Judge.

[Endorsed]: Filed March 22, 1943. [26]

[Title of Court.]

Criminal No. 16633

Abortion

TERRITORY OF HAWAII,

vs.

PETER L. YOUNG and HILDA M. NOZAWA,  
Defendants.

At Term. 2:30 o'clock P.M., Friday, February  
19, 1943.

Present: Hon. Carrick H. Buck, First Judge,  
Presiding. O. Sezenevsky, Clerk. S. H. Minns,  
Reporter.

COURT'S RULING ON MOTION FOR SEVER-  
ANCE AND SEPARATE TRIAL

John E. Parks, Esq., Assistant Public Prosecutor.

Joseph V. Esposito, Esq., Counsel for Peter L.  
Young, one of the Defendants.

The Court granted the Motion of Peter L. Young,  
one of the defendants, herein, by J. V. Esposito, his  
attorney, for Severance and Separate Trial, filed  
herein on the 23rd day of October, 1942.

Counsel for the Territory excepted to the Court's  
ruling.

By Order of the Court.

O. SEZENEVSKY,  
Clerk. [27]

[Title of Court.]

Friday, Feb. 26, 1943

At Term—2:00 p.m.

Present: Hon. A. M. Cristy, Second Judge, Presiding. D. M. Feder, Clerk. R. N. Linn, Reporter.

[Title of Cause.]

Counsel: C. E. Cassidy, Esq., Public Prosecutor. J. V. Esposito, Esq., for Defendants. Defendants in Person.

Defendants were called to the Bar and after being questioned pleaded Not Guilty to the charge, which plea was duly noted and entered by the Court.

The case was set for trial on March 15 at 9:00 a.m.

By the Court.

/s/ D. M. FEDER

Clerk.

Tuesday, March 16, 1943

At Term—9:00 O'Clock A.M.

Present: The Court. R. N. Linn, Reporter.

Counsel: Same.

### TRIAL BY JURY

Counsel being ready to proceed with the trial of the above entitled case, the Court instructed the Clerk to draw the jury:

- |                     |                      |
|---------------------|----------------------|
| 1. Paul K. Strauch  | 7. A. R. Wyeth       |
| 2. J. C. Richardson | 8. A. L. De Crow     |
| 3. Wesley Rickard   | 9. Otto C. Meyer     |
| 4. E. A. Brenner    | 10. William E. Brede |
| 5. Ching Fat        | 11. Lawrence Santos  |
| 6. Robert Edgar     | 12. J. G. Walsh      |

who were duly sworn in together with the other jurors in the Courtroom.

Counsel examined the jurors and passed them for cause.

Mr. John E. Parks, counsel for prosecution, exercising his first peremptory challenge, excused Mr. Ching Fat, who was replaced by (13) Mr. Chun Sung Ching.

Counsel for defendant, exercising his first peremptory challenge, excused Mr. Robert Edgar, who was replaced by (14) Paul H. Anderson.

Counsel for prosecution, exercising his second peremptory challenge, excused Mr. Chung Sung Ching, who was replaced by (15) Frank M. Almeida.

Counsel for defendant, exercising his second peremptory challenge, excused Mr. Lawrence Santos, who was replaced by (16) A. Burger.

Counsel for prosecution, exercising his third and last peremptory challenge, excused Mr. E. A. Brenner, who was replaced by (17) Wilbur M. Spencer.

Counsel for defendant stated that the jury was satisfactory.

The Court instructed the Clerk to swear in the jury to try the case:

- |                      |                      |
|----------------------|----------------------|
| 1. Paul K. Strauch   | 7. A. R. Wyeth       |
| 2. J. C. Richardson  | 8. A. L. De Crow     |
| 3. Wesley Rickard    | 9. Otto C. Meyer     |
| 4. Wilbur M. Spencer | 10. William E. Brede |
| 5. Frank M. Almeida  | 11. A. Burger        |
| 6. Paul H. Anderson  | 12. J. G. Walsh      |

At 9:52 a.m. the Court recessed. [29]

At 9:58 a.m. the Court reconvened, whereupon



counsel for prosecution delivered his opening statement to the jury and disclosed what the prosecution intended to prove in this case.

Counsel for defendant reserved his opening statement until after the close of prosecution's case.

At 10:09 a.m. counsel for prosecution called as a witness (1) Miss Rose Dolim, who, upon being duly sworn, testified.

Counsel for prosecution offered in evidence the following exhibits which were received by the Court and marked as follows:

Prosecution's Exhibit "A"

Savings Account Pass Book #14277 in the name of Mrs. Rose D. Kinkelie showing a withdrawal on August 8, 1942, of \$60.00.

Prosecution's Exhibit "B"

Marriage License taken out in the names of Joseph Franklin Sudduth and Rose Dolim issued in Honolulu, T. H., on July 30, 1942, by Leila L. Rankin, Marriage License Agent.

Prosecution's Exhibit "C"

Letter, dated Aug. 8, 1942, from Dr. Peter L. Young addressed—To Whom It May Concern: This certifies that Rose Dolim is under my medical supervision for menorrhagia. Yours truly—Dr. P. L. Young.

Prosecution's Exhibit "D"

Small Box of Pills with pencilled notation "2 every 2 hours" and also a small envelope containing 4 small green pills with the notation on the front of said envelope—"1 tablet every 3 hrs."

## Prosecution's Exhibit "E"

Wyeth's Ergoklomin purified solution of Ergot and also a small box containing 6 pills with the notation—"1 tablet every 3 hours." [30]

## Prosecution's Exhibit "F"

Bottle of "Bo-car-al" being a Hygenic Powder and a non-irritating astringent, deodorant and manufactured by Sharp & Dohme.

At 10:55 a.m. the Court recessed.

At 11:02 a.m. the Court reconvened, whereupon counsel for prosecution offered in evidence,

Bottle of Cough Mixture with the following directions—"2 teaspoons every 2 hours" and bearing Dr. Peter L. Young's name, business address and office hours thereon,

which was received by the Court and marked Prosecution's Exhibit "G."

At 11:15 a.m. cross examination

At 11:30 a.m. the Court recessed.

At 1:30 p.m. the Court reconvened; further cross examination.

At 2:12 p.m. the Court recessed.

At 2:17 p.m. the Court reconvened, whereupon counsel for prosecution called as a witness (2) Mrs. Olive Dolim Rodrigues, who, upon being duly sworn, testified.

At 2:30 p.m. cross examination.

At 2:42 p.m. redirect examination.

At 2:43 p.m. recross examination.

At 2:45 p.m. counsel for prosecution called as a

witness (3) Detective Anthony Paul, who, upon being duly sworn, testified.

At 2:55 p.m. the Court recessed.

At 3:00 p.m. the Court reconvened, whereupon counsel for prosecution offered in evidence,

Statement made by Miss Rose Dolim at Pau-  
ahi [31] 2 Ward, Room 214, Queen's Hospital  
at 4:00 p.m. on August 22, 1942,

which was received by the Court and marked Prosecution's Exhibit "H."

At 3:07 p.m. cross examination.

At 3:13 p.m. redirect examination.

At 3:14 p.m. recross examination.

At 3:15 p.m. re-direct examination.

At 3:16 p.m. re-cross examination.

At 3:18 p.m. the Court continued the further trial of this case until Wednesday, March 17, 1943 and adjourned at term.

By the Court.

/s/ L. P. HOLT

Clerk.

Wednesday, March 17, 1943

At Term—9:00 O'Clock A.M.

Present: The Court. R. N. Linn, Reporter.  
Counsel: Same.

## FURTHER TRIAL

Counsel being ready to proceed with the further trial of the above entitled case, stipulated the presence of the jury and the defendant.

At 9:01 a.m. counsel for prosecution called as a witness (4) Dr. Gilbert Halpern, who, upon being sworn, testified.

At 9:15 a.m. cross examination.

At 9:39 a.m. counsel for prosecution called as a witness (5) Itsuko Murakami, who, upon being duly sworn, testified. [32]

At 9:43 a.m. cross examination.

The witness was requested to read the statement of Miss Rose Dolim (heretofore offered as Prosecution's Exhibit "H") from his shorthand notes while counsel checked the transcript.

At 9:46 a.m. further cross examination.

At 9:48 a.m. counsel for prosecution called as a witness (6) Police Officer Albert Felix, who, upon being duly sworn, testified.

Counsel for prosecution offered for Identification and in Evidence respectively the following exhibits which were received by the Court and marked as follows:

Prosecution's Exhibit "I" for Identification

Statement of Dr. Peter L. Young dated Aug. 22, 1942, made at the Detective Division of the Honolulu Police Department.

Prosecution's Exhibit "J"

Orange colored card purporting to be the "Patient Card" of Miss Rose Dolim, 1261 Central St., taken from the files of Dr. Peter L. Young.

At 10:01 a.m. cross examination.

At 10:03 a.m. the Court recessed.

At 10:19 a.m. the Court reconvened, whereupon counsel for prosecution called as a witness (7) Police Officer Robert K. Kadota, who, upon being duly sworn, testified.

At 10:24 a.m. the Court recessed to allow counsel for defendant to check the defendant's statement to the Police.

At 10:53 a.m. the Court reconvened; cross examination. [33]

Counsel for defendant asked leave of the Court to have the witness read from his shorthand notes and that counsel check the transcript relative to Dr. Young's statement to the Police. The Court granted the request. Counsel for defendant called the court's attention to an apparent discrepancy in the words "aerial hemmorrhage" appearing on page 7 of said statement.

At 11:29 a.m. the witness concluded reading his shorthand notes at which time counsel for prosecution offered the statement in evidence. The Court received the exhibit in evidence and gave it the same identifying mark, to-wit, Prosecution's Exhibit "I."

At 11:30 a.m. counsel for prosecution rests.

At 11:31 a.m. the Court continued the further trial of this case until Thursday, March 18, 1943, at 9:00 o'clock a.m. and adjourned at term.

By the Court.

/s/ JOSEPH L. COCKETT  
Clerk

Thursday, March 18, 1943

At Term—9:00 O'Clock A.M.

Present: The Court. R. N. Linn, Reporter.  
Counsel: Same.

### FURTHER TRIAL

Counsel being ready to proceed with the further trial of the above entitled case, stipulated the presence of the jury and the defendant.

At 9:01 a.m. counsel for defendant delivered his opening statement to the jury.

At 9:05 a.m. counsel for defendant called as a [34] witness (8) Dr. Peter L. Young, who, upon being duly sworn, testified.

At 9:48 a.m. cross examination

At 10:02 a.m. the Court recessed.

At 10:10 a.m. the Court reconvened; further cross examination.

At 11:27 a.m. the Court recessed.

At 1:30 p.m. the Court reconvened, whereupon counsel for defendant called as a witness (9) Dr. Joseph W. Lam, who, upon being duly sworn, testified.

At 1:47 p.m. cross examination.

At 1:56 p.m. redirect examination.

At 2:06 p.m. the Court interrogated the witness.

At 2:09 p.m. recross examination.

At 2:13 p.m. re-direct examination.

At 2:14 p.m. counsel for defendant called as a witness (10) Dr. Hong Quon Pang, who, upon being duly sworn, testified.



At 2:24 p.m. cross examination.

At 2:30 p.m. the Court interrogated the witness.

At 2:31 p.m. redirect examination.

At 2:33 p.m. recross examination.

At 2:34 p.m. the Court recessed.

At 2:38 p.m. the Court reconvened, whereupon Dr. Peter L. Young resumed the witness stand under further cross examination.

At 3:30 p.m. the Court continued the further [35] trial of this case until Friday, March 19, 1943, at 9:00 o'clock a.m. and adjourned at term.

By the Court.

/s/ L. R. HOLT

Clerk.

Friday, March 19, 1943

At Term—9:00 O'Clock A.M.

Present: The Court. R. N. Linn, Reporter.  
Counsel: Same.

### FURTHER TRIAL

Counsel being ready to proceed with the further trial of the above entitled case, stipulated the presence of the jury and the defendant.

At 9:01 a.m. Dr. Peter L. Young resumed the witness stand under further cross examination.

At 9:12 a.m. redirect examination.

Counsel for defendant offered for Identification,

Five sheets consisting of pages 291, 292, 293, 294, 295, 296, 297, 298, 299 and 300 taken from the text book "Midwifery by Ten Teachers,"

edited by Comyns Berkeley, H. Russell Andrews, J. S. Fairbairn and published by Edward Arnold & Co.—London—1925,

which was received by the Court and marked Defendant's Exhibit "1" for Identification.

At 9:35 a.m. recross examination.

At 9:36 a.m. defense rests.

At 9:37 a.m. the Court called counsel to the bench to discuss the question of instructions.

At 9:38 a.m. the Court excused the jury until Monday, March 22, 1943, at 8:30 o'clock a.m. and requested counsel to meet with the Court at 10:00 a.m. this day to settle the matter of instructions.

## INSTRUCTIONS

At 10:00 a.m. counsel met with the Court in chambers to settle the instructions in this case. The following instructions were taken up and ruled upon, to-wit:

### Prosecution's Requested Instructions:

No. 1—Given by agreement.

No. 2—Given by agreement.

No. 3—Given by agreement.

No. 4—Given over objection.

No. 5—Given over objection.

No. 6—Given over objection.

No. 7—Withdrawn.

No. 8—Given by agreement.

No. 9—Given over objection.

No. 10—Given by agreement.

Defendant's Requested Instructions:

No. 1—Refused.

No. 2—Given by agreement.

No. 3—Given by agreement.

No. 4—Given by agreement.

No. 5—Refused as covered.

No. 6—Given by agreement.

No. 7—Given by agreement.

No. 8—Given by agreement.

No. 9—Withdrawn.

No. 10—Refused.

No. 11—Refused.

No. 12—Given by agreement as modified.

No. 13—Withdrawn.

By the Court.

/s/ L. R. HOLT

Clerk.

Monday, March 22, 1943

At Term—8:30 O'Clock A.M.

Present: The Court. R. N. Linn, Reporter.  
Counsel: Same.

**FURTHER INSTRUCTIONS**

Counsel for defendant submitted Defendant's Requested [37] Instruction #10 as modified with the elimination of the words "or health."

Counsel for prosecution submitted Prosecution's Requested Instruction #11 which was received and marked—Given by Agreement in lieu of Defendant's Instruction #10.

**FURTHER TRIAL**

Counsel being ready to proceed with the further trial of the above entitled case, stipulated the presence of the jury and the defendant.

At 8:37 a.m. Mr. John E. Parks, counsel for prosecution, delivered his opening argument to the jury.

At 9:19 a.m. counsel for prosecution concluded his argument to the jury.

At 9:20 a.m. the Court recessed.

At 9:25 a.m. the Court reconvened, whereupon counsel for defendant argued.

At 10:37 a.m. counsel for defendant concluded his argument to the jury, whereupon the Court recessed.

At 10:42 a.m. the Court reconvened, whereupon counsel for prosecution delivered his closing argument to the jury.

At 11:04 a.m. upon the conclusion of counsel for prosecution's argument, the Court read the instructions to the jury.

At 11:17 a.m. the Court concluded the reading of the instructions to the jury, whereupon counsel

for defendant excepted to the giving of Prosecution's [38] Requested Instructions numbered 4, 5, 6 and 9 and further excepted to the Court's refusal to give Defendant's Requested Instructions numbered 1, 5 and 11.

At 11:19 a.m. the Court instructed the Clerk to take the jury to lunch and immediately upon its return to start its deliberations in the Courtroom of the Second Division.

At 12:15 p.m. the jury returned from lunch and started its deliberation.

At 1:53 p.m. the jury returned the following verdict:

We the Jury in the above entitled cause, find the Defendant Guilty as charged.

/s/ PAUL H. ANDERSON  
Foreman.

Honolulu, T. H., March 22nd, 1943.

The Court ordered the Verdict filed.

Counsel for defendant excepted to the verdict as being contrary to the law, the evidence and the weight of the evidence and gave notice of appeal and his intention to sue out a Writ of Error.

At 1:55 p.m. the Court adjourned at term.

By the Court.

/s/ L. P. HOLT  
Clerk. [39]

In the Supreme Court of the Territory  
of Hawaii

No. 2544

TERRITORY OF HAWAII,

Defendant in error,

vs.

PETER L. YOUNG,

Plaintiff in error.

APPLICATION FOR WRIT OF ERROR

To the Clerk of the Supreme Court:

Please issue a writ of error in the above case to the Clerk of the Circuit Court, First Circuit, Territory of Hawaii, on behalf of said defendant, returnable to the Supreme Court.

Dated: June 18, 1943.

PETER L. YOUNG,

By /s/ FRED PATTERSON

/s/ E. J. BOTTS

His Attorneys

[Endorsed]: Filed June 19, 1943. [41]

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[Title of Supreme Court and Cause.]

WRIT OF ERROR

Territory of Hawaii, Greeting:

To the Clerk of the Circuit Court of the First Circuit, Territory of Hawaii:

Application having been made on behalf of Peter L. Young for a Writ of Error in the above entitled



cause, you are commanded forthwith to send to the Supreme Court the record in said cause.

Witness the Honorable Samuel S. Kemp, Chief Justice of the Supreme Court, this 19 day of June, 1943.

/s/ CHAS. H. K. HOLT

Clerk of the Supreme Court

The execution of the above Writ of Error appears by the certified record attached hereto.

Dated: Honolulu, T. H., August 14, 1943.

/s/ SYBIL DAVIS

Clerk, First Circuit Court,  
Territory of Hawaii. [44]

I hereby certify that on the 19th day of June, 1943, I received the original and copies of Application for Writ of Error, Writ of Error, and Assignment of Errors in the above entitled cause.

/s/ JOHN R. DESHA

Asst Public Prosecutor

[Endorsed]: Filed June 19, 1943. [45]

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[Title of Supreme Court and Cause.]

### ASSIGNMENT OF ERRORS

Comes now Peter L. Young, Plaintiff in Error, and files an assignment of errors upon which he

will rely on appeal to the Supreme Court of the Territory of Hawaii.

### I.

The Court erred in sustaining prosecution's objection to question asked Rose Dolim, complaining witness, by defendant on cross-examination, as follows:

Question: . . . Were you arrested for fornication, for a crime?

Mr. Parks: That is objected to . . .

The Court: Objection sustained.

To which ruling defendant excepted (Tr. p. 45-46).

### II.

The Court erred in overruling motion by defendant to strike certain evidence adduced when Anthony Paul, a police officer, was called by the prosecution. (Tr. p. 95). Having testified on direct examination that after defendant was arrested, he was ordered to discharge him from custody, he was asked on cross-examination if he was not discharged because the police believed the defendant's story and not the complaining witness' story. The colloquy follows:

Question: Isn't it a fact that he was discharged because he was treating her for hemorrhagia, and whether an abortion happened it was for saving life?

Answer: No sir, because we suspected him of being one of several abortionists in this town, and . . . (interrupted).

Mr. Esposito: I move that that be stricken as not responsive (Tr. p. 96).

Said motion was denied and exception then and there duly taken.

### III.

The Court erred in overruling objection to question asked defendant on cross-examination by the prosecution in the following proceeding:

Question: Have you ever been convicted of drunkenness?

Answer: Yes, once; once in a lifetime.

Question: And was that right after this case? Was that right after Rose Dolim went to the hospital?

Mr. Esposito: Your Honor, I object . . .

The Court: Objection overruled.

Answer: About a month after . . .

Question: That you were convicted of drunkenness? Isn't it a fact, doctor, that the abortion did not become inevitable until after you had gotten the \$150.00? (Tr. p. 289-290)

Defendant's objection to said question being overruled, the defendant then and there did except. [47]

### IV.

The Court erred in instructing the jury, at the request of the prosecution, as follows:

#### Territory's Instruction No. 4

You are instructed that it is no defense under the law to the crime of abortion as charged in the indictment that Rose Dolim solicited, requested or

consented to have an abortion performed upon her body even if you so find the fact to be.

To the giving of the instruction above set out, the defendant, at the conclusion of the charge of the Court, in the presence of the jury and before the jury retired, duly noted an objection.

## V.

The Court erred in instructing the jury, at the request of the prosecution, as follows:

### Territory's Instruction No. 5

The jury is instructed that an actual miscarriage is not necessary under the statute with which the defendant is charged in this case. The crime is complete if a person maliciously, without lawful justification, administers any poison or noxious thing to a woman, when pregnant, in order to procure her miscarriage, or maliciously uses an instrument on a woman, when pregnant, with intent to procure her miscarriage. It is wholly immaterial whether or not a miscarriage actually results.

Sec. 6232, R. L. of H. 1935. 1 Amer. Jur. 136, Sec. 12.

To the giving of the instruction above set out, the defendant, at the conclusion of the charge of the Court, in the presence of the jury and before the jury retired, duly noted an exception. [48]

## VI.

The Court erred in instructing the jury, at the request of the prosecution, as follows:

## Territory's Instruction No. 6

The court further instructs you that our statute also provides that everyone shall be presumed to intend the natural and plainly probable consequences of his acts.

Sec. 5358, R. L. of H., 1935.

To the giving of the instruction above set out, the defendant, at the conclusion of the charge of the Court, in the presence of the jury and before the jury retired, duly noted an exception.

## VII.

The Court erred in instructing the jury, at the request of the prosecution, as follows:

## Territory's Instruction No. 9

I further instruct you that the burden of proof is upon the Territory and the law presumes the defendant to be innocent, and this presumption continues and attends him at every stage of the case until it has been overcome by evidence which proves him guilty to your satisfaction and beyond a reasonable doubt. And in this connection, I instruct you that the doubt which will entitle the defendant to an acquittal must be a reasonable doubt, not a conjured-up doubt, such a doubt as you might conjure up to acquit a friend, but a doubt that you could give a reason for.

A reasonable doubt is not a slight doubt, not a probable doubt, not a possible doubt, not a conjectural doubt, not an imaginary doubt, not a doubt

of the absolute certainty of the guilt of the accused, because everything relating to human affairs and depending upon moral evidence is open to conjectural or imaginary doubt, and because absolute certainty is not required by law. The real question is whether after hearing the evidence and from the evidence [49] you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty and if you have such belief so formed, it is your duty to convict, and if you have not such belief so formed it is your duty to acquit.

To the giving of the instruction above set out, the defendant, at the conclusion of the charge of the Court, in the presence of the jury and before the jury retired, duly noted an exception.

#### VIII.

The Court erred in refusing to give defendant's requested instruction No. 1, reading as follows:

##### Instruction No. 1

You are instructed to find the defendant, Peter L. Young, not guilty.

#### IX.

The Court erred in refusing to give defendant's requested instruction No. 5, reading as follows:

##### Instruction No. 5

A reasonable doubt is that state of the mind which after a full comparison and consideration of all of the evidence both for the prosecution and



the defense, leaves the minds of the jury in that condition that they cannot say that they feel an abiding faith amounting to a moral certainty from the evidence in the case, that the defendant is guilty of the crime as laid in the indictment. If you have such doubt and if your conviction of the defendant's guilt as laid in the indictment does not amount to a moral certainty from the evidence in the case, then you must find the defendant not guilty.

### X.

The Court erred in refusing to give defendant's requested instruction No. 11, reading as follows:

#### Instruction No. 11

I instruct you that the statutes [50] on abortion are intended to prevent and punish the destroying of embryo human life, the germs of human life before birth, in the course of nature, and would not apply to acts to procure the miscarriage of a woman having a dead fetus in her womb.

Com. of Mass. v. Brown, 121 Mass. 69.

Wherefore, the said Plaintiff-in-error prays that said above entitled cause may be reversed and remanded with instruction to the trial court as to further proceedings, and for such other and further relief as may be proper in the premises.

PETER L. YOUNG

/s/ By FRED PATTERSON

/s/ E. J. BOTTS

His Attorneys

## NOTICE

To the Prosecuting Attorney, City and County of  
Honolulu, Territory of Hawaii:

You are hereby notified that application for a writ of error in the above entitled matter has been filed.

/s/ FRED PATTERSON

/s/ E. J. BOTTS

Attorneys for Plaintiff in  
Error.

Dated June 19th, 1943.

[Endorsed]: Filed June 19, 1943. [51]

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[Title of Supreme Court and Cause.]

## OPINION OF THE COURT

Hon. A. M. Cristy, Judge.

Submitted June 22, 1945. Decided July 25, 1945.

Kemp, C. J., Peters and Le Baron, JJ.

Criminal law—instructions and reasonable doubt.

It is not error, in instructing upon reasonable doubt, to include the definition “a doubt that you could give a reason for.”

Witnesses — credibility — cross examination for purposes of impeachment—former conviction of crime.

It is not error in the exercise of the right to impeach a witness, pursuant to the provisions of Revised Laws of Hawaii 1935, section 3831, to fix the time of the conviction of a witness by reference

to the time of an occurrence, evidence of which is before the jury.

Abortion—nature and elements of the offense.

A woman aborted is “with child” within the meaning of that term contained in Revised Laws of Hawaii 1935, section 6232, defining the crime of abortion, [53] although the fetus prior to expulsion has lost its vitality so that it could not mature into a living child. [54]

#### OPINION OF THE COURT BY PETERS, J.

This is a writ of error to review a judgment of conviction upon verdict of a jury of the crime of abortion. The following errors have been specified:

1. Error in instructing the jury, in defining a reasonable doubt, that such a doubt was one for which a reason could be given;

2. Error in permitting the prosecution, when defendant admitted having been convicted of a certain offense, to question him further over objection, with respect to said offense;

3. Error in refusing to instruct the jury at defendant's request that our criminal statute relating to abortion does not apply to acts to procure the miscarriage of a woman having a dead fetus in her womb.

The errors specified will be considered seriatim.

1. The language to which objection is made is but a part of the instruction given by the court

upon burden of proof, presumption of innocence and reasonable doubt. The instruction in full reads as follows: "I fruther instruct you that the burden of proof is upon the Territory and the law presumes the defendant to be innocent, and this presumption continues and attends him at every stage of the case until it has been overcome by evidence which proved him guilty to your satisfaction and beyond a reasonable doubt. And in this connection, I instruct you that the doubt which will entitle the defendant to an acquittal must be a reasonable doubt, not a conjured-up doubt, such a doubt as you might conjure up to acquit a friend, but a doubt that you could give a reason for. [55]"

"A reasonable doubt is not a slight doubt, not a probable doubt, not a possible doubt, not a conjectural doubt, not an imaginary doubt, not a doubt of the absolute certainty of the guilt of the accused, because everything relating to human affairs and depending upon *mortal* evidence is open to conjectural or imaginary doubt, and because absolute certainty is not required by law. The real question is whether after hearing the evidence and from the evidence you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty and if you have such belief so formed, it is your duty to convict and if you have not such belief so formed it is your duty to acquit."

The cases are in conflict upon the subject. The expression "a doubt for which a reason can be given," in more or less varying form, is found in instructions upon reasonable doubt given by trial

judges in federal courts.<sup>1</sup> In the cases cited in note one the propriety of the instruction was not questioned. In some jurisdictions similar instructions have been sustained.<sup>2</sup> In others they were held to constitute prejudicial error.<sup>3</sup> And in still others,

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1. " \* \* \* a doubt for which a reason may be assigned." *U. S. v. Stephens*, 27 Fed. Cas. 1314 (#16392). " \* \* \* a doubt for which a good reason arising from the evidence, can be given." *United States v. Johnson*, 26 Fed. 82, 685. " \* \* \* a doubt for which a good reason can be given, which reason must be based on the evidence, or the want of evidence." *United States v. Jackson*, 29 Fed. 503, 504; *United States v. Cassidy*, 67 Fed. 698, 782.

2. " \* \* \* a doubt for which you can give a reason." *Wallace v. State*, 41 Fla. 547, 580. It is " \* \* \* a doubt which must arise from the evidence, or lack of evidence, and for which some reason can be given." *Griggs v. United States*, 9 C. C. A. 158, 572, 578. " \* \* \* a doubt for which some good reason arising from the evidence can be given." *The People v. Guidici*, 100 N. Y. 503, 510, 3 N. E. 493, 495. " \* \* \* a doubt for which a reason can be given, based on the evidence in the case. \* \* \*." *Butler v. The State*, 102 Wis. 368, 78 N. W. 590, 591, citing *Emery and another v. The State*, 101 Wis. 627, 78 N. W. 145. " \* \* \* such a doubt as the juror is able to give a reason for." *State v. Grant*, 20 S. D. 168, 105 N. W. 97, 99, citing *State v. Serenson*, 7 S. D. 277, 64 N. W. 130.

3. " \* \* \* a reasonable doubt is one for which a reason could be given based on the evidence or want of evidence in the case." *Pettine v. Territory of New Mexico*, 201 Fed. 489, 495 (C. C. A. 8th Cir.); *Ayer v. Territory of New Mexico*, 201 Fed. 497, 498 (C. C. A. 8th Cir.). "A reasonable doubt is such a doubt as the jury are able to give a reason for." *State of Iowa v. Cohen*, 108 Iowa, 208, 78 N. W. 857, 858; *Siberry v. The State*, 133 Ind. 677, 33 N. E. 681, 684. "It must be a ground of doubt for which a reason can



though criticized, the error, if any, was considered harmless.<sup>4</sup>

In the Michigan case the court made the following comment: "Conceding, in this case, that the exposition of the phrase by the circuit judge was not strictly accurate, yet it is apparent that it could have produced no practical consequence in this case." The Ohio court observed: "This objection does not impress us as of the highest consequence." The Oregon court said in conclusion: "The particular language in question may be, and no doubt is, subject to the criticism that it does not define, but needs defining, but we do not think it could have misled or perplexed the jury when considered in

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be given, which reason must be based upon the evidence or want of evidence." *Owens v. United States*, 130 Fed. 279, 283 (C. C. A. 9th Cir.). " \* \* \* a doubt for the having of which the juror can give a reason derived from the testimony." *Carr v. State*, 23 Neb. 749, 751, citing *Cowan v. State*, 22 Neb. 519; see also *Childs v. State*, 34 Neb. 236, 51 N. W. 837. " \* \* \* a doubt \* \* \* for which you as reasonable men can give a good and sufficient reason." *State v. Rosenberg*, 97 N. J. 430, 433, 118 Atl. 207, 208; see also *State v. Parks*, 96 N. J. 360, 363. " \* \* \* a doubt you can give a reason for." *Abbott v. Territory*, 20 Okla. 119, 94 Pac. 179.

" \* \* \* a doubt arising out of the facts and circumstances of the case in maintaining which you can give some good reason." *People v. Stubenvoll*, 62 Mich. 329, 334, 28 N. W. 883. " \* \* \* a doubt for which you can give a reason." *State v. Sauer*, 38 Minn. 438, 439, 38 N. W. 355. " \* \* \* a doubt as a juror can give a reason for." *State v. Morey*, 25 Ore. 241, 36 Pac. 573, 577. " \* \* \* a doubt that you as a juror can give a reason for." *Morgan v. The State*, 48 Ohio 371, 27 N. E. 710, 712.



connection with the remainder of the instruction. If every criminal case is to be reversed for some technical inaccuracy in the definition of a reasonable doubt, then indeed the 'administration of justice becomes impracticable.' "

The question involved arises from the difficulty encountered by trial judges in presenting to juries in criminal cases instructions for their guidance in applying the rule of proof beyond a reasonable doubt. The degree of proof necessary to convict is complementary to the presumption of innocence and unless understood the presumption of innocence is of little protection to the accused. To instruct a jury merely that the defendant is presumed innocent until he is proved guilty beyond a reasonable doubt, while sufficient in itself to accord to him his substantial rights, has been thought by many courts, including those of Hawaii, to be insufficient as a guide to juries in arriving at their ultimate conclusions and they have attempted to define the term. These instructions have taken the form of a definition of the adjective "reasonable," the inclusion of instruction of what are not reasonable doubts and the time-honored test enunciated by Chief Justice Shaw in *Commonwealth v. Webster*, reported in 5 Cush. (Mass.) 295, 320.

The instruction in controversy is of this type. From long-continued use and uniform approval by this court when before it for review, it has assumed the dignity of a stock instruction. It came before this court in substantially the same form in 1889 in the case of *The King v. Ahop*, 7 Haw. 556, 560,

and was approved, the author of the opinion eruditely observing that the instruction was taken from the notes to *Commonwealth v. McKie*, 1 Leading Crim. Cases, pages 320, 321. It was also before this court in *Territory v. [58] Robello*, 20 Haw. 7, decided in 1910, and in *Ter. v. Buick*, 27 Haw. 28, decided in 1923, when again it was approved. While it does not appear that in any of those cases the particular error herein specified was advanced or discussed, the language giving rise to the present objection as an integral part of the definition of reasonable doubt was necessarily considered. It has also been subject to the judicial scrutiny of this court upon writ of error in three capital cases since the effective date of Laws of 1931, chapter 42, section 2, making it obligatory in case of a sentence of death to review the evidence to determine if the interests of justice require a new trial, whether the insufficiency of the evidence is assigned as error or not.<sup>5</sup>

To the legal mind it is difficult to formulate a satisfactory definition of the term "reasonable doubt." The difficulty seems to stem from the futile attempt to define the obvious. But instructions are addressed to the lay and not the legal mind. And measured by the purposes sought to be attained, the instruction complained of is, as a whole, as good as can be devised to convey to the lay mind the ordinarily accepted definition of reasonable doubt.

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<sup>5</sup>No. 2257, *Territory v. Corum*, No. 2466, *Territory v. Alcosiba*, No. 2454, *Territory v. Gagarin*.

“Burden of proof” is a term employed to indicate upon whom rests the duty of persuasion by proof. To persuade another is to convince such other that a thing is so. If convinced, such other possesses a settled belief that the thing is so. In criminal cases the burden of proof is directed to the persuasion of the trier of the facts of the guilt of the defendant of the offense charged. But due to the presumption [59] of innocence accorded persons accused of crime, the trier of the facts, before he may say he is convinced, must be satisfied of the defendant’s guilt beyond all reasonable doubt. Hence it is that the measure of persuasion is spoken of as proof beyond a reasonable doubt, and the measure of the intensity of belief of the trier of the facts becomes the measure of persuasion. It is to communicate intelligibly to jurors a method of self-analysis for one’s belief that instructions upon reasonable doubt are directed.

It may be taken as conceded by the defendant that with the elimination of the language “but a doubt that you could give a reason for” the instruction correctly states the law. The negative definitions contained therein unquestionably conform to the accepted definitions of what is not a reasonable doubt. They, similarly as the language objected to, are calculated to define the adjective “reasonable.” Isolated phrases must be construed in the light of the context in which they appear. The meaning to be ascribed to the phrase “a doubt you could give a reason for” must necessarily be construed in the light of the negative definitions

given and as so construed harmonizes with the instruction as a whole. A doubt that one can give a reason for is unquestionably a reasonable doubt. A doubt that one cannot give a reason for is within the category of the negative definitions contained in the instruction. Both positive and negative definitions are directed to the mental operation of the jurors. It is a mental and not a demonstrable doubt to which the phrase refers. Instructions upon reasonable doubt are not given to supply individual jurors with material to meet adverse arguments of their fellow jurors. Nor are they calculated to enable the [60] individual juror to criticise the mental operations of another juror. A juror is not required to give his reasons to other jurors for his mental reactions or conclusions. The instruction was well calculated to assist the jury in applying the test, with which it concludes: "The real question is whether after hearing the evidence and from the evidence you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty." What to one man might be a slight, probable, possible, conjectural or imaginary doubt may, in all seriousness, be to another a reasonable doubt. Each juror, in his own way, is presumably making an honest effort to determine whether he entertains in his own mind a doubt of the defendant's guilt and if so whether such doubt is a conjectural or imaginary doubt or is one that has its basis in reason, one for which he can give a reason and therefore reasonable. If the intensity of his belief is such that he can say

he has an abiding belief amounting to a moral certainty of the guilt of the defendant, then the degree of persuasion has been met; otherwise not. Whatever the form of words employed, if the concepts of the language used are consistent with the ordinarily accepted meaning of the term "reasonable doubt" the instruction meets the test of definition. As said by Professor Wigmore: "The truth is that no one has yet invented or discovered a mode of measurement for the intensity of human belief. Hence there can be yet no successful method of communicating intelligibly to a jury a sound method of self-analysis for one's belief. If this truth be appreciated, the Courts will cease to treat any particular form of words as necessary or decisive in the law for that purpose; for the Law cannot expect to do what Logic and Psychology have not yet done."<sup>6</sup> [61]

2. The following colloquy occurred upon cross-examination of the defendant as a witness on his own behalf:

"Q. Have you ever been convicted of drunkenness?

"A. Yes, once; once in a lifetime.

"Q. Once in a lifetime, you say, Doctor?

"A. Yes.

"Q. And that was right after this case? That was right after (name of prosecutrix omitted) went to the hospital? (Objection; objection overruled.)

"A. About a month after."

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<sup>6</sup>Wigmore, *Ev.* (3d ed.) § 2497, p. 325.



The prosecution urges that by this evidence there was presented to the jury the details of the offense of which the defendant had been convicted.

Whether the specification of error urged was preserved below is open to considerable doubt. No grounds of objection were alleged. Nor does it appear from the record what reasons, if any, were assigned for such objection. Moreover, no exception was alleged to the ruling of the court. Hence the error specified comes within the prohibition of Revised Laws of Hawaii, 1935, section 3563, as construed by this court in *Ter. v. Gagarin*, 36 Haw. 1.

Nevertheless, we have considered the question and find it to be without merit. It is competent under the provisions of Revised Laws of Hawaii, 1935, section 3831, for the prosecution to question the defendant upon cross-examination as to whether he had been convicted of any indictable or other offense.<sup>7</sup> His answer "once in a lifetime" not only implied infrequency but remoteness. The extent that the credibility of the defendant might be impaired by former conviction of an indictable or other offense would be affected accordingly as such conviction was recent or remote. It is, therefore, legitimate [62] for the prosecution to fix the time of conviction. This is sought to do by reference to an incident with which the jury was familiar; that is, the time when the prosecutrix went to the hospital. But it was to the time of the defendant's conviction and not to the time of his being drunk that the question was directed. The time of

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<sup>7</sup>*Ter. v. Goo Wan Hoy*, 24 Haw. 741.



the conviction of offense is not a detail of the offense in the objectionable sense of improper cross-examination of the details of an indictable or other offense of which the witness had been convicted.

3. The court refused to give the following instruction, requested by the defendant: "I instruct you that the statutes on abortion are intended to prevent and punish the destroying of embryo human life, the germs of human life before birth, in the course of nature, and would not apply to acts to procure the miscarriage of a woman having a dead fetus in her womb."

We need only concern ourselves with that portion of the instruction that declares that the statutes on abortion would not apply to acts to procure the miscarriage of a woman having a dead fetus in her womb. If an incorrect statement of the law, the instruction was properly refused in toto.

Revised Laws of Hawaii, 1935, section 6232, defines the crime of abortion as follows: "Whoever maliciously, without lawful justification, administers, or causes or procures to be administered any poison or noxious thing to a woman when with child, in order to produce her miscarriage, or maliciously uses any instrument or other means with like intent, shall, if the woman be then quick with child, be punished by a fine not exceeding one thousand dollars and imprisonment at hard labor [63] not more than five years; and if she be then not quick with child, shall be punished by a fine not exceeding five hundred dollars, and imprisonment at hard labor not more than two years."

The gravamen of the crime of abortion, as de-

fined by section 6232, *supra*, is the malicious administration of drugs to or the use of instruments upon a woman with child in order to produce a miscarriage.

The term "with child" is not defined by the lexicographers. It is included in the definitions of the noun "pregnancy" and of the adjective "pregnant" and is often used synonymously with the latter term. The noun "miscarriage" is defined as "the act of bringing forth before the natural time; a premature birth; with women, the delivery of the fetus before the twenty-eighth week of pregnancy."<sup>8</sup> The verb "miscarry" is defined "to bring forth in child-birth prematurely; abort"<sup>9</sup>; "to suffer untimely delivery; to bring forth young prematurely; to give birth to a fetus which is not viable."<sup>10</sup> Where the abortion is for criminal purposes the word "miscarriage" carries the added implication of the unlawful interference with the course of pregnancy with the intent of destroying the product of conception.

The noun "miscarriage" obviously implies that the woman aborted is with child and the term "with child" qualifying [64] the noun "woman" might quite properly have been omitted from the statute. It apparently is present for the dual purpose of excluding from the condemnation of the statute

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<sup>8</sup>Funk & Wagnalls New Standard Dictionary (1929 ed.).

<sup>9</sup>Funk & Wagnalls New Standard Dictionary (1929 ed.).

<sup>10</sup>The Century Dictionary & Cyclopedia.

misconceived abortions, that is, abortions where the woman is not actually with child, and of defining the period within which the crime may be committed, that is, from the moment the womb is instinct with embryo life and gestation has begun until expulsion or delivery.<sup>11</sup> The latter consideration is confirmed by the degrees of punishment attached to the crime of abortion accordingly as the woman is quick with child or not. (§ 6232, *supra*.)

While the term "with child" similarly as the adjective "pregnant" ordinarily denotes vitality of the fetus, it also connotes a physical condition following conception and continuing until expulsion or delivery, irrespective of whether the fetus prior to expulsion has lost its vitality, so that it could not mature into a living child. The adjective "pregnant" has been so construed.<sup>12</sup> Nor do the definitions and connotations of the noun "miscarriage" exclude abortions of feti which prior to expulsion have lost their vitality so that they could not mature into living children. On the contrary, according to its ordinarily accepted meaning it has reference to premature birth, either spontaneous or induced, irrespective of the prior vitality of the fetus. [65]

Plaintiff in error places great reliance upon the case of *Commonwealth v. Wood*, 11 Gray (Mass.) 85. The statute under which the defendant was

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<sup>11</sup>*Mills v. Commonwealth*, 13 Pa. (1 Harris) 631, 632.

<sup>12</sup>*State v. Howard*, 32 Vt. 380, 398; *State v. Tippi*, 89 Ohio 35, 105 N. E. 75, 77; *State v. Cox*, 197 Wash. 67, 84 P. (2d) 357, 361.

prosecuted is not available in the library but is quoted in *Commonwealth v. Brown*, 14 Gray (Mass.) 419.

Although differently from our statute defining abortion, the Massachusetts statute used the adjective "pregnant" instead of "with child" in describing the woman aborted, it is otherwise sufficiently similar to our local statute to resort to decisions of that State construing its provisions as precedents. But the opinion of the court in the Wood case does not support the thesis that in order that the crime of abortion be complete the fetus must have had vitality up to the time of miscarriage. The question presented for review was whether the trial court had improperly refused an instruction upon lawful justification, a defense recognized by the Massachusetts statute, similarly as Revised Laws of Hawaii, 1935, sections 6232 and 6233. Under section 6232 the abortion to be criminal must be "without justification." Section 6233 absolves persons from criminal liability for abortion where the means used are for the purpose of saving the life of the woman. The trial court had refused an instruction that a lawful justification "would exist if the child with which Sarah Chaffie (the woman aborted) was pregnant was not a live child." And in considering the alleged error the appellate court, [6] among other things said: "If the defendant meant to say it would be a legal justification to show that the fetus with which the woman was pregnant had lost its vitality so it could not mature into a living child, we think the

decision correct and that the jury should have been so instructed, if there was any evidence before the jury upon the subject. But the bill of exceptions not only fails to state that any such evidence was given at the trial or offered, but expressly negatives the fact. If there had been evidence that the fetus had lost its vitality it might have been the duty of the judge to say directly to the jury that if they so found, the case was not within the statute. Upon the case by the bill of exceptions there was no occasion for any direction on the matter."

It would seem from the foregoing quoted language of the court that the vitality of the fetus was pertinent only as it might affect the defense of lawful justification and that the court did not hold as claimed by plaintiff in error that the woman was not pregnant within the meaning of the statute if the fetus had lost its vitality so that it could not mature into a living child. The Wood case is not persuasive to say the least. Not alone is it not in point, but is mere dicta and whatever implications it possessed they were neutralized by the subsequent amendment of the statute. (See *Commonwealth v. Taylor*, 132 Mass. 261, and *Commonwealth v. Surles*, 165 Mass. 59, 42 N. E. 502.)

The jury was fully instructed upon what constituted lawful justification within the exception of section 6232, *supra*, and upon the provisions of section 6233. The legal effect of these statutory provisions are not involved in the consideration of



the instruction, the subject of this specification of error.

Judgment affirmed.

F. PATTERSON and

E. J. BOTTS,

For Plaintiff in Error.

W. Z. FAIRBANKS,

Public Prosecutor, and

J. E. PARKS,

Assistant Public Prosecutor,  
for Defendant in Error.

[Endorsed]: Filed July 25, 1945. [68]

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[Title of Supreme Court and Cause.]

### ORDER

Good cause appearing therefor, it is hereby ordered that plaintiff in error may have up to and including the 1st day of October, 1945, within which time to prepare and file with the clerk of the Circuit Court, 9th Circuit, the record on appeal in the the above entitled matter.

Dated: August 6, 1945.

/s/ S. B. KEMP,

Chief Justice, Supreme Court,  
Territory of Hawaii.

[Endorsed]: Filed Aug. 6, 1945. [70]



In the Supreme Court of the Territory of Hawaii

No. 2544

THE TERRITORY OF HAWAII,

Defendant in Error,

vs.

PETER L. YOUNG,

Plaintiff in Error.

JUDGMENT ON WRIT OF ERROR

In the above entitled cause, pursuant to the opinion of the above entitled court rendered and filed on July 25, 1945, the assignments of error are overruled, the writs denied and the verdict and judgment below sustained.

Dated: Honolulu, Hawaii, August 13th, 1945.

By the Court:

[Seal]     /s/ LEOTI V. KRONE,  
Clerk.

Approved:

/s/ S. B. KEMP,  
Chief Justice, Supreme Court.

Received a copy of the above Judgment this  
13th day of August, 1945.

/s/ W. Z. FAIRBANKS,  
Public Prosecutor, City and  
County of Honolulu.

[Endorsed]: Filed Aug. 13, 1945. [72]

[Title of Supreme Court and Cause.]

### NOTICE OF APPEAL

1. Name and address of plaintiff in error: Peter L. Young, 3775 Old Pali Road, Honolulu, T. H.

2. Name and address of attorneys for plaintiff in error: Fred Patterson, McCandless Building, and E. J. Botts, Stangenwald Building, Honolulu, T. T.

3. Offense: Violation of Section 11652, Revised Laws of Hawaii, 1945, viz. the crime of abortion.

4. Date of Judgment: Supreme Court of Hawaii judgment Aug. 13, 1945.

5. Brief description of judgment or sentence: Tried before a jury in the Circuit Court of the First Judicial Circuit, Territory of Hawaii, found guilty by the jury March 26, 1943, and thereafter sentenced to imprisonment by the Honorable A. M. Cristy, presiding judge, for a term of two years.

6. Plaintiff in error is released on bail.

7. Grounds for appeal: Plaintiff in error claims that the trial judge erred in instructing the jury upon reasonable doubt that it was "a doubt that you could give a [74] reason for."

I, the above named plaintiff in error, hereby appeal to the United States Circuit Court of Appeals

for the Ninth Circuit from the judgment above mentioned on the grounds set forth herein.

/s/ PETER L. YOUNG,  
Plaintiff in Error.

Dated: August 13th, 1945.

Receipt of a copy of the foregoing Notice of Appeal is acknowledged this 13th day of August, 1945.

/s/ W. Z. FAIRBANKS,  
Public Prosecutor.

[Endorsed]: Filed Aug. 13, 1945. [75]

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In the Circuit Court of Appeals  
For the Ninth Circuit

THE TERRITORY OF HAWAII,  
Defendant in Error,

vs.

PETER L. YOUNG,  
Plaintiff in Error.

### ASSIGNMENT OF ERRORS

Comes now Peter L. Young, plaintiff in error in the above entitled matter, and files the following assignment of errors upon which he will rely in the prosecution of his appeal from the decision of the Supreme Court of the Territory of Hawaii.

Plaintiff in error was indicted by the grand jury for the crime of abortion, to-wit, Section 11652,

Revised Laws of Hawaii, 1945, and thereafter was tried for said crime in the Circuit Court of the First Judicial Circuit, Territory of Hawaii, and at the conclusion of the evidence, the presiding judge gave the jury the following instruction:

“I further instruct you that the burden of proof is upon the Territory and the law presumes the defendant to be innocent, and this presumption continues and attends him at every stage of the case until it has been overcome by evidence which proves him guilty to your satisfaction and beyond a reasonable doubt. And in this connection, I instruct you that the doubt which will entitle the defendant to an acquittal must be a reasonable doubt, not a conjured up doubt, such as you might conjure up to acquit a friend, but a doubt that you could give a reason for. [77]

“A reasonable doubt is not a slight doubt, not a probable doubt, not a possible doubt, not a conjectural doubt, not an imaginary doubt, not a doubt of the absolute certainty of the guilt of the accused, because everything relating to human affairs and depending upon moral evidence is open to conjectural or imaginary doubt, and because absolute certainty is not required by law. The real question is whether after hearing the evidence and from the evidence you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty and if you have such belief so formed, it is your duty to convict, and if you have not such belief so formed it is your duty to acquit;” and plaintiff in error says that the trial court erred

in instructing the jury that a reasonable doubt is "a doubt that you could give a reason for," and assigns as error the decision and opinion of the Supreme Court of the Territory of Hawaii in holding and deciding that said instruction was not error.

Wherefore, plaintiff in error prays that the decision and judgment of the Supreme Court may be reversed, and for such further relief as to the Court may seem just and proper.

Dated: Honolulu, Hawaii, August 13th, 1945.

PETER L. YOUNG

By FRED PATTERSON and  
E. J. BOTTS

/s/ Per E. J. BOTTS

His Attorneys

Receipt of a copy of the foregoing Assignment of Errors is acknowledged this 13th day of August, 1945.

/s/ W. Z. FAIRBANKS

Public Prosecutor

[Endorsed]: Filed Aug. 13, 1945. [78]

In the Supreme Court of the  
Territory of Hawaii

No. 2544

THE TERRITORY OF HAWAII,

Defendant in Error,

vs.

PETER L. YOUNG,

Plaintiff in Error.

CLERK'S STATEMENT OF DOCKET  
ENTRIES

1. Indictment for crime of abortion, viz. violation of Section 11652, Revised Laws of Hawaii, 1945, by the Grand Jury of the Territory of Hawaii, on October 15, 1942.

2. Arraignment before judge of the Circuit Court, First Judicial Circuit, October 16 and 17, 1942.

3. Plea of not guilty made and entered February 26, 1943.

4. Tried before a jury beginning March 16, 1943.

5. Verdict of guilty returned by jury March 22, 1943.

6. Judgment and sentence of trial court on March 26, 1943. Defendant being sentenced to imprisonment in Oahu Prison for a term of two years.

7. Writ of error issued out of the Supreme



Court of the Territory of Hawaii to the said Circuit Court on June 19, 1943.

8. Decision of the Supreme Court rendered July 25, 1945.

9. Judgment of Supreme Court filed and entered August 13, 1945.

Dated: August 13, 1945.

[Seal]      /s/ LEOTI V. KRONE

Clerk, Supreme Court of the  
Territory of Hawaii.

[Endorsed]: Filed Aug. 13, 1945. [80]

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[Title of Supreme Court and Cause.]

PRAECIPE

To the Clerk of the Supreme Court:

Please cause to be prepared and transmitted to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, San Francisco, California, certified copies of the following:

1. The indictment.
2. Instructions given by the court to the jury.
3. Trial court's minutes.
4. Writ of error from Supreme Court to Circuit Court, First Circuit.
5. Assignment of Errors in proceeding before Supreme Court.

6. Opinion of Supreme Court.
7. Judgment of Supreme Court.
8. Notice of Appeal and Appeal to Circuit Court of Appeals, Ninth Circuit.
9. Assignment of Errors.
10. Clerk's (Supreme Court) statement of docket entries.

Dated: August 13th, 1945.

PETER L. YOUNG

By FRED PATTERSON and  
E. J. BOTTS

Per /s/ E. J. BOTTS

His Attorneys

[Endorsed]: Filed Aug. 13, 1945. [81]

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[Title of Supreme Court and Cause.]

CLERK'S CERTIFICATE

I, Leoti V. Krone, clerk of the supreme court of the Territory of Hawaii, do hereby certify that the foregoing documents are full, true and correct copies of the originals on file in the above entitled court and cause, as follows:

1. Indictment, filed October 15, 1942;
2. Instructions given by the court to the jury;
3. Trial court's minutes;
4. Writ of Error from Supreme Court to cir-

cuit court first circuit (includes Application for Writ of Error) filed June 19, 1943;

5. Assignment of Errors in proceeding before Supreme Court, filed June 19, 1943;

6. Opinion of supreme court, filed July 25, 1945;

7. Order extending time for record on appeal to 9th circuit court of appeals, filed August 6, 1945;

8. Judgment of supreme court, filed August 13, 1945; [83]

9. Notice of Appeal and Appeal to 9th circuit court of appeals, filed August 13, 1945;

10. Assignment of Errors, filed August 13, 1945;

11. Supreme Court Clerk's statement of docket entries, filed August 13, 1945;

12. Praecipe, filed August 13, 1945.

I further certify that the cost of the foregoing transcript of record on appeal to the ninth circuit court of appeals is \$69.65, and that the said amount has been paid by E. J. Botts, one of the attorneys for plaintiff in error.

In Witness Whereof, I have hereunto set my hand and the seal of the supreme court of the Territory of Hawaii, at Honolulu, Hawaii, this 6th day of September, 1945.

[Seal]

LEOTI V. KRONE

Clerk, Supreme Court, Territory of Hawaii. [84]

[Endorsed]: No. 11144. United States Circuit Court of Appeals for the Ninth Circuit. Peter L. Young, Appellant, vs. Territory of Hawaii, Appellee. Transcript of Record. Upon Appeal from the Supreme Court for the Territory of Hawaii.

Filed September 24, 1945.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals  
for the Ninth Circuit.

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In the United States Circuit Court of Appeals  
For the Ninth Circuit

No. 11144

PETER L. YOUNG,

Appellant,

vs.

THE TERRITORY OF HAWAII,

Appellee.

DESIGNATION OF PARTS OF RECORD TO  
BE PRINTED AND POINTS RELIED ON

Comes now Peter L. Young, appellant, by Fred Patterson and E. J. Botts, his attorneys, and hereby requests that the record be printed in its en-

tirety, and appellant adopts as his points on appeal the assignment of errors appearing in the record.

Dated: Honolulu, Hawaii, October 22, 1945.

PETER L. YOUNG,

Appellant

By FRED PATTERSON and

E. J. BOTTS

Per [Illegible]

His Attorneys

Copy served on William Z. Fairbanks, Public Prosecutor, by mail this 22nd day of October, 1945.

[Illegible]

[Endorsed]: Filed Oct. 24, 1945. Paul P. O'Brien, Clerk.





No. 11,144

IN THE  
United States Circuit Court of Appeals  
For the Ninth Circuit

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PETER L. YOUNG,

*Appellant,*

VS.

TERRITORY OF HAWAII,

*Appellee.*

BRIEF FOR APPELLANT.

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FRED PATTERSON,

McCandless Building, Honolulu, T. H.,

E. J. BOTTS,

Stangenwald Building, Honolulu, T. H.,

*Attorneys for Appellant.*

FILED

JUL 10 1945

PAUL P. O'BRIEN,



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No. 11,144

IN THE

# United States Circuit Court of Appeals

For the Ninth Circuit

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PETER L. YOUNG,

*Appellant,*

VS.

TERRITORY OF HAWAII,

*Appellee.*

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## BRIEF FOR APPELLANT.

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This appeal is by defendant in a criminal action from a final judgment of the Supreme Court of the Territory of Hawaii.

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### STATEMENT OF JURISDICTION.

Appellant was indicted by the Grand Jury of the Territory of Hawaii, First Circuit, violation Section 11652, Revised Laws of Hawaii, 1945, i.e. the crime of abortion. He was tried in the Circuit Court, First Circuit, and convicted (R. 27). Following his conviction and within the time allowed by statute (Chapter 186, Revised Laws of Hawaii, 1945), he prosecuted a writ of error to the Supreme Court of the Territory of Hawaii. The Supreme Court had jurisdiction (Sec.

9551, Revised Laws of Hawaii, 1945). The final judgment of the Supreme Court of the Territory of Hawaii affirmed the judgment of the said Circuit Court (R. 53). Appellant duly appealed to this court (R. 55). The jurisdiction of this court to review the final judgment of the Supreme Court of the Territory of Hawaii is sustained by Section 128 of the Judicial Code (28 U.S.C.A., Sec. 225).

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### **STATEMENT OF THE CASE.**

Appellant was convicted of violating Section 11652, Revised Laws of Hawaii, 1945. This section, which in the 1935 revised laws was Section 6232, reads as follows:

“Whoever maliciously, without lawful justification, administers, or causes or procures to be administered any poison or noxious thing to a woman when with child, in order to produce her miscarriage, or maliciously uses any instrument or other means with like intent, shall, if the woman be then quick with child, be punished by a fine not exceeding one thousand dollars and imprisonment at hard labor not more than five years; and if she be then not quick with child, shall be punished by a fine not exceeding five hundred dollars, and imprisonment at hard labor not more than two years.”

The indictment against appellant charged that he “maliciously, wilfully, unlawfully and feloniously, and without lawful justification, did use and employ



an instrument and a certain noxious substance, a more particular description of which are to the Grand Jury unknown, by then and there forcing said instrument and said noxious substance into the body and womb of a certain woman, to-wit, one Rose Dolim, she, the said Rose Dolim, being then and there pregnant and not quick with child, with intent \* \* \* to use the said instrument and noxious substance as afore-said to produce and procure the miscarriage of the said Rose Dolim \* \* \*

While the indictment charged that Peter L. Young did the acts complained of in association with Hilda M. Nozawa, a severance was granted and Peter L. Young was tried alone (R. 14).

When the evidence was in, the court instructed the jury and, over the objection of appellant, gave the following instruction:

“I further instruct you that the burden of proof is upon the Territory and the law presumes the defendant to be innocent, and this presumption continues and attends him at every stage of the case until it has been overcome by evidence which proves him guilty to your satisfaction and beyond a reasonable doubt. And in this connection, I instruct you that the doubt which will entitle the defendant to an acquittal must be a reasonable doubt, not a conjured up doubt, such as you might conjure up to acquit a friend, but *a doubt that you could give a reason for.*”

On writ of error to the Supreme Court, appellant challenged this instruction, the giving of which by the trial court he assigned as error.

**SPECIFICATION OF ASSIGNED ERRORS RELIED ON.**

The particular objection to the instruction quoted above is found in the last sentence of the first paragraph thereof which reads as follows: "And in this connection, I instruct you that the doubt which will entitle the defendant to an acquittal must be a reasonable doubt, not a conjured up doubt, such as you might conjure up to acquit a friend, but *a doubt that you could give a reason for.*" Appellant has assigned this instruction, given as aforesaid, as error.

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**ARGUMENT.**

The instruction complained of, restricting a reasonable doubt to one which may be "boxed in" so to speak, places the burden on defendant to develop in the evidence not only a reasonable doubt, but a reasonable doubt of a kind a juror can give a reason for; in effect, a demonstrable doubt. It ignores the impalpable element in evidence which may leave a juror, for no assignable reason, unwilling to accord the prosecution's case the accolade of truth; yet he is told in effect under this instruction he must convict anyway. Though he may not be able in good conscience to do so, he must convict because he can furnish no specific, tangible reason to explain his reaction to testimony which has left his mind in doubt on the issue of defendant's guilt.

Both State and Federal Courts have reversed criminal cases where the trial court, departing from the

classic definition of "reasonable doubt" given by Chief Justice Shaw in *Commonwealth v. Webster*, 8 Cush. 293, limited such doubts to a class having a definite expressable reason.

The Circuit Court of the 8th Circuit, twice in a relatively short time, reversed the Supreme Court of the Territory of New Mexico, which had held the trial court did not commit reversible error in giving such an instruction to a jury. In the first case, *Pettine v. Territory of New Mexico*, 201 Fed. 489, the court instructed the jury:

"\* \* \* that a reasonable doubt is one for which a reason could be given based on the evidence or want of evidence in the case."

Notwithstanding this instruction, the Supreme Court of New Mexico sustained the conviction, but on appeal the Circuit Court reversed this decision. Circuit Judge Sanborn, who delivered the opinion for the court, said:

"In a criminal case the presumption of innocence accompanies the defendant throughout the trial. The burden is on the government to overcome this presumption, to produce evidence that will satisfy the minds of the jury beyond a reasonable doubt of the guilt of the accused. The burden is upon the prosecution to furnish to the jury by the evidence it produces, sound reasons for the conviction of the defendant, reasons that shall produce and maintain in their minds an abiding conviction of his guilt to a moral certainty. Now to say that a doubt of the guilt of an

accused person which a juror may indulge is not a reasonable doubt unless he can give a reason for it based on the evidence or want of it is to reverse this established rule, and to put upon the accused the burden of furnishing the jury with a reason for his acquittal; for, if the juror must give a reason for his doubt, he must give a sound reason, or this new rule is idle and ineffective. If no juror who has a doubt of the guilt of the accused may lawfully vote for his acquittal unless he can give a sound reason for his doubt based on the evidence or the want of it, the question immediately arises whether this reason must be sound in his own opinion only, or in the opinion of his fellow jurors, or of the judge, and, once adopt this rule and instructions on this subject must inevitably multiply and add dialectics and confusion to the rule and its application. The ability to give sound reasons for their doubts or their beliefs is not given to many men, and every prudent and thoughtful man at once recognizes the fact that in the graver and more important affairs of his own life doubts for which he can formulate no convincing reason often induce him to act or to refuse to act. To require every person accused of crime to present such a state of evidence at his trial that every juror can give a sound reason based on the testimony for his doubt of his guilt before he may vote for his acquittal places too heavy a burden on the accused. It destroys the rule of reasonable doubt and substitutes for a reasonable doubt a demonstrable doubt logically and conclusively sustained by the evidence or the want of it. The court below was in error when it placed this heavy burden upon the de-

fendant, and charged the jury that a reasonable doubt was one for which a reason could be given founded on the evidence or want of it."

In the second case from New Mexico (*Ayer v. Territory*, 201 Fed. 497), the Supreme Court recognized the instruction as wrong but concluded defendant had not been prejudiced thereby. The Circuit Court, taking issue, said: "\* \* \* because this instruction destroys the rule of reasonable doubt, substitutes for a reasonable doubt a demonstrative doubt, logically and conclusively sustained by the evidence or want of it and places too heavy a burden on defendant, it is error."

The Nebraska Supreme Court, in *Cowan v. State*, 22 Neb. 519, reversed a case where the trial court has instructed the jury that a reasonable doubt was one for which the jury could give a reason. The Supreme Court took issue with this definition; said it was calculated to mislead the jury. "The definition of reasonable doubt", said the Nebraska Supreme Court, "given by Chief Justice Shaw in *Commonwealth v. Webster*, 8 Cush. 293, is, that the evidence must be such as to 'establish the truth of the fact to a reasonable and moral certainty, a certainty that convinces and directs the understanding and satisfies the reason of those who are bound to act conscientiously upon it.' This seems to be the correct definition of a reasonable doubt."

A conviction was reversed in *State v. Parks*, 115 A. 305, 96 N. J. Law 360, because an instruction was



given substantially the same as the one given in the case at bar. "Reasonable doubt is not necessarily a result to be worked out by the rules of logic", the New Jersey Supreme Court said, "it may likewise legitimately arise from the impressions, often incapable of analysis, made upon the minds of jurors by the evidence and the witnesses \* \* \* The same or similar criticism applies to a further instruction in this case, that reasonable doubt is a '*doubt arising upon the evidence for which you, as reasonable men, can give a good and sufficient reason*'. Both instructions contained harmful error." Conviction was reversed.

In another New Jersey case (*State v. Rosenberg*, 97 N. J. Law 430, 118 Atl. 207), the court dealt at length with this erroneous definition of reasonable doubt. Said the court:

"It is further insisted on behalf of Plaintiff in error that the learned judge erred in charging the jury on the question of reasonable doubt. He charged that a reasonable doubt was 'a doubt respecting his (defendant's) guilt arising upon the evidence, or from the lack of evidence, for which you as reasonable men can give a good and sufficient reason.' It is observable that the learned judge makes the existence of a reasonable doubt depend upon the condition that where a juror's mental state, after hearing the evidence, is such that he can give a good and sufficient reason for the doubt he entertains. This view is antagonistic to the settled law of this state. We have adopted the doctrine of reasonable doubt as defined by Chief Justice Shaw in *Commonwealth v. Webster*, 5 Cush. (Mass.) 295, at page 320, 52 Am. Dec.



711; *Donnelly v. State*, 26 N. J. Law 601 at page 615. The test there furnished as to when a reasonable doubt may be properly said to have arisen is stated as follows:

“ ‘Reasonable doubt is not a mere possible doubt. It is that state of the case which after the entire comparison and consideration of all the evidence, leaves the minds of the jurors in that condition that they cannot say they feel an abiding conviction to a moral certainty of the truth of the charge.’ ”

See *State v. Linker*, 94 N. J. Law 412, 111 Atl.

35.

“ ‘Keeping this definition in view, as to what in law constitutes a reasonable doubt, it is quite plain that the test to be adopted by the jurors to determine whether such reasonable doubt exists according to the decisions of our highest tribunals, is not whether the jurors can give a good and sufficient reason for their doubt, but the arising of such reasonable doubt is predicated solely upon the state of mind produced upon the jurors, by a comparison and consideration of all the evidence in the case, so that they cannot say that they feel an abiding conviction amounting to a moral certainty of the truth of the charge.’ ”

---

### CONCLUSION.

The cases we have cited, it is respectfully submitted, represent the weight of authority. The cases to the contrary relied on in the opinion of the Supreme Court of Hawaii do not commend themselves

to reason or logic; they concede the instruction is wrong, but contend the error was "harmless". Yet the jurors were told for all practical purposes that they could not convict merely because they had a reasonable doubt as to defendant's guilt, but that they had to have a special kind of reasonable doubt, to-wit, one they could give a reason for. We say that is not good law, that on its face it is prejudicial; and that there should be a reversal in this case for that reason.

Dated, Honolulu, T. H.,  
December 27, 1945.

Respectfully submitted,

FRED PATTERSON,

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Per FRED PATTERSON,

*Attorneys for Appellant.*

Receipt of a copy of the foregoing brief is hereby  
acknowledged this 27th day of December, 1945.

JOHN E. PARKS,  
Deputy City and County Prosecutor  
Honolulu, T. H.



No. 11144

IN THE  
**United States Circuit Court of Appeals**  
FOR THE NINTH CIRCUIT

---

PETER L. YOUNG,

*Appellant,*

VS.

TERRITORY OF HAWAII,

*Appellee.*

---

Upon Appeal from the Supreme Court of the Territory of Hawaii

**TERRITORY'S ANSWERING BRIEF**

FILED

1911

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No. 11144

IN THE

**United States Circuit Court of Appeals**  
**FOR THE NINTH CIRCUIT**

---

PETER L. YOUNG,

*Appellant,*

vs.

TERRITORY OF HAWAII,

*Appellee.*

---

**TERRITORY'S ANSWERING BRIEF**

---

**STATEMENT OF JURISDICTION**

The appellant has not shown that this Court has or should take jurisdiction under Section 128 of the Judicial Code, Amended, (28 U.S.C.A. Sec. 225).

**STATEMENT OF THE CASE**

This whole appeal merely involves nine words *italicized* in the instruction hereinafter set forth. The facts of guilt of the appellant are not in question.

The Supreme Court of the Territory of Hawaii states:

"It may be taken as conceded by the defendant that with the elimination of the language 'but a doubt that you could give a reason for' the instruction correctly states the law." (Record p. 43.)

The appellant on page 3 of his brief sets forth only a *portion* of Territory's Instruction No. 9. The entire instruction defining "reasonable doubt" is as follows:

**"TERRITORY'S INSTRUCTION NO. 9**

"I further instruct you that the burden of proof is upon the Territory and the law presumes the defendant to be innocent, and this presumption continues and attends him at every stage of the case until it has been overcome by evidence which proves him guilty to your satisfaction and beyond a reasonable doubt. And in this connection, I instruct you that the doubt which will entitle the defendant to an acquittal must be a reasonable doubt, not a conjured-up doubt, such a doubt as you might conjure up to acquit a friend, but *a doubt that you could give a reason for*.

A reasonable doubt is not a slight doubt, not a probable doubt, not a possible doubt, not a conjectural doubt, not an imaginary doubt, not a doubt of the absolute certainty of the guilt of the accused, because everything relating to human affairs and depending upon mortal evidence is open to conjectural or imaginary doubt, and because absolute certainty is not required by law. The real question is whether after hearing the evidence and from the evidence you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty and if you have such belief so formed, it

is your duty to convict and if you have not such belief so formed it is your duty to acquit." (Record pp. 8-9.) (Emphasis ours.)

### SUMMARY OF ARGUMENT

1. **THE APPELLANT HAS NOT SHOWN THAT THIS COURT HAS OR SHOULD TAKE JURISDICTION OF THIS CASE UNDER SECTION 128 OF THE JUDICIAL CODE, AMENDED, (28 U.S.C.A. SEC. 225).**

(a) Obviously a treaty or statute of the United States or any authority exercised thereunder is not involved herein. The only question is whether or not the Territory's instruction on "reasonable doubt" violates the "due process" clause of the Fifth and Fourteenth Amendments of the Constitution of the United States.

(b) The due process clause of the Fifth and Fourteenth Amendments means the same thing except the Fifth Amendment applies to the federal government and its instrumentalities. The Fourteenth Amendment applies to the several states.

*Bowles v. Willingham*, 321 U.S. 503, 64 S. Ct. 641, 88 L. Ed. 892, 905

*Hamilton v. Kentucky Distilleries & W. Co.*, 251 U.S. 146, 40 S. Ct. 106, 64 L. Ed. 194, 199

*United States v. Darby*, 312 U.S. 100, 61 S. Ct. 451, 85 L. Ed. 609

*Hibben v. Smith*, 191 U.S. 310, 24 S. Ct. 88, 48 L. Ed. 195, 201

Taylor: Due Process of Law, Sec. 49, p. 107

Taylor: Due Process of Law, Sec. 14, p. 23

(c) The case does not involve any federal question but simply a general rule of law.

*Kimbrel v. Territory of Hawaii* (C.C.A. 9th),  
41 Fed. (2d) 740, 740-741

*Barrington v. Missouri*, 205 U.S. 483, 27 S. Ct.  
582, 51 L. Ed. 890

*The City and County of San Francisco v. Itsell*,  
133 U.S. 65, 10 S. Ct. 241, 33 L. Ed. 570, 571

*Giles v. Little*, 134 U.S. 645, 10 S. Ct. 625, 33  
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*City and County of San Francisco v. Jane Scott*,  
111 U.S. 768, 4 S. Ct. 688, 28 L. Ed. 593

*United States v. Thompson*, 93 U.S. 586, 23 L.  
Ed. 982

*Allen v. McVeigh*, 107 U.S. 433, 2 S. Ct. 558,  
27 L. Ed. 572

*West v. State of Louisiana*, 194 U.S. 258, 24 S.  
Ct. 650, 48 L. Ed. 965

(d) The due process clause of the Fifth and Fourteenth Amendments does not prohibit the Territory of Hawaii from enforcing its criminal laws under appropriate statutory provisions and common law doctrines. It does not permit a test by this Court of every ruling made by a territorial court in the course of a trial.

*Buchalter v. New York*, 319 U.S. 427, 63 S. Ct. 1129, 87 L. Ed. 1492, 1495-1496

Taylor: Due Process of Law, Sec. 551, p. 824

(e) Substantial or material error in an instruction to the jury in a criminal case in a court of the Territory of Hawaii does not necessarily violate the due process clause of the Fifth or Fourteenth Amendments.

*Buchalter v. New York*, 319 U.S. 427, 63 S. Ct. 1129, 87 L. Ed. 1492, 1495-1496

*Davis v. State of Texas*, 139 U.S. 651, 11 S. Ct. 675, 35 L. Ed. 300

Taylor: Due Process of Law, Sec. 551, p. 824

(f) The presumption of innocence is as fundamental a concept of our law as the doctrine of reasonable doubt. But failure to instruct on the presumption of innocence has been held not to constitute a denial of due process under the Fourteenth Amendment.

*Howard v. Fleming*, 191 U.S. 126, 24 S. Ct. 49, 48 L. Ed. 121, 125

**2. ASSUMING ARGUENDO THAT A FEDERAL QUESTION IS INVOLVED HEREIN, THE WRIT OF ERROR SHOULD BE DISMISSED BECAUSE SUCH FEDERAL QUESTION IS NOT SUBSTANTIAL.**

This Court has already decided the issue involved herein adversely to the appellant.

*Griggs v. United States*, (C.C.A. 9th), 158 Fed. 572, 577-578

*Louie Ding v. United States*, (C.C.A. 9th), 246 Fed. 80

The appeal is therefore frivolous.

*Equitable Life Ass. Society of the United States v. Brown*, 187 U.S. 308, 311, 23 S. Ct. 123, 47 L. Ed. 190, 192

The appellant's appeal has not presented a substantial federal question.

*Fukunaga v. Territory of Hawaii*, (C.C.A. 9th), 33 Fed. (2d) 396, 397

*Stanworth v. United States*, (C.C.A. 9th), 45 Fed. (2d) 158, 159

3. **THE CIRCUIT COURT OF THE FIRST JUDICIAL CIRCUIT, TERRITORY OF HAWAII, DID NOT ERR IN GIVING TO THE JURY TERRITORY'S INSTRUCTION NO. 9 ON REASONABLE DOUBT.**

(a) The language assigned as error in said instruction has been used by trial courts of Hawaii in their charge to juries on reasonable doubt since 1889.

*King v. Abop* (1889), 7 Haw. 556, 560-561

*Territory of Hawaii v. Robello* (1910), 20 Haw. 7, 22-23, 31

*Territory of Hawaii v. Buick* (1923), 27 Haw. 28, 36, 40-41

(b) The United States Circuit Court of Appeals for the Ninth Circuit has already settled the issue raised herein adversely to the appellant.

*Griggs v. United States*, (C.C.A. 9th), 158 Fed. 572, 577-578

*Louie Ding v. United States*, (C.C.A. 9th), 246 Fed. 80, 83



(c) Territory's Instruction No. 9 considered and construed in toto is not erroneous.

*Mansfield v. United States*, (C.C.A. 8th), 76 Fed. (2d) 224, 230

(d) The appellant's criticism herein is "hyper-critical."

*Marshall v. United States*, (C.C.A. 2nd), 197 Fed. 511, 512-513; Certiorari denied, 226 U.S. 207, 33 S. Ct. 112, 57 L. Ed. 379

(e) The language complained of herein or similar language has been used and upheld by a large number of federal courts.

*United States v. Woods*, (C.C.A. 2nd), 66 Fed. (2d), 262, 265

*Murphy v. United States*, (C.C.A. 3rd), 33 Fed. (2d), 896; Certiorari denied, 280 U.S. 584, 50 S. Ct. 35, 74 L. Ed. 634

*Sotello v. United States*, (C.C.A. 5th), 256 Fed. 721, 723-724

*Colbeck v. United States*, (C.C.A. 7th), 10 Fed. (2d) 401, 404; Certiorari denied, *Colbeck v. United States*, 271 U.S. 662, 46 S. Ct. 474, 70 L. Ed. 1138

*United States v. Butler*, Cas. No. 14,700, 1 Hughes 457, 25 Fed. Cas. 213, 226

*United States v. Stevens*, Cas. No. 16,392, 2 Hask. 164, 27 Fed. Cas. 1312, 1314

*United States v. Johnson*, 26 Fed. 682, 685

*United States v. Jackson*, 29 Fed. 503

*United States v. Cassidy*, 67 Fed. 698, 782

*United States v. Guthrie*, 171 Fed. 528, 532

*United States v. Wilson*, 176 Fed. 806, 809

*United States v. Hill*, 1 Fed. (2d), 954, 956

*United States v. Sussman*, 37 Fed. Supp. 294

*Maupin v. United States*, (C.C.A. 4th), 258  
Fed. 607

(f) The instructions given by the trial court on the presumption of innocence, burden of proof and reasonable doubt fully protected the appellant.

Territory's Instruction No. 9 (Record pp. 8-9)

Territory's Instruction No. 11 (Record p. 9)

Defendant's Instruction No. 2 (Record p. 10)

Defendant's Instruction No. 3 (Record pp. 10-  
11)

Defendant's Instruction No. 4 (Record p. 11)

Defendant's Instruction No. 7 (Record p. 12)

(g) The term "reasonable doubt" is self-defining. Territory's Instruction No. 9 could not therefore be prejudicial.

*United States v. Breen*, (C.C.A. 2nd), 96 Fed.  
(2d) 782, 784

(h) The language used, considering the entire instruction, was favorable to the appellant and "is sustained by respectable authority."

*Miles v. United States*, 103 U.S. 304, 312, 26 L. Ed. 481, 484

*Dunbar v. United States*, 156 U.S. 185, 15 S. Ct. 325, 39 L. Ed. 390, 395

(i) The state courts are not as uniform as the federal courts in upholding instructions containing substantially the same language as that objected to herein, but the majority rule follows the federal cases cited herein.

*Butler v. State*, 102 Wis. 364, 78 N.W. 590, 592

*Emery v. State*, 101 Wis. 627, 78 N.W. 145, 152-155

*State v. Patton*, 66 Kan. 486, 71 Pac. 840, 841

*State v. Fox*, 116 Kan. 180, 225 Pac. 1042

*People v. Guidici*, 100 N.Y. 503, 3 N.E. 493, 495-496

*People v. Lagroppo*, 90 App. Div. 219, 86 N.Y.S. 116, 126

*State v. Serenson*, 7 S.D. 277, 64 N.W. 130, 132

*State v. Grant*, 20 S.D. 164, 105 N.W. 97, 99

*State v. Sonnenschein*, 37 S.D. 585, 159 N.W. 101, 106

*State v. Merry*, 136 Me. 243, 8 Atl. (2d) 143, 153

*State v. Butler*, 148 S.C. 495, 146 S.E. 418, 419

*Bryant v. State*, 197 Ga. 641, 30 S.E. (2d) 259, 269

*State v. Jefferson*, 43 La. Ann. 995, 10 So. 199,  
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*King v. State*, 17 Ala. App. 536, 87 So. 701,  
702-703

*Wallace v. State*, 41 Fla. 547, 26 So. 713, 723-  
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*State v. Dunn*, 159 Wash. 608, 294 Pac. 217,  
218-219

*People v. Grove*, 284 Ill. 429, 120 N.E. 277, 281

*State v. Gilbert*, 8 Idaho 346, 69 Pac. 62, 63-64

*State v. Morey*, 25 Ore. 241, 36 Pac. 573, 577-  
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*People v. Steubenvoll*, 62 Mich. 329, 28 N.W.  
883, 884, 885

*State v. Sauer*, 38 Minn. 438, 38 N.W. 355

*People v. Yun Kee*, 8 Cal. A. 82, 96 Pac. 95

*Mansfield v. United States*, 76 Fed. (2d) 224,  
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#### ARGUMENT

1. THE APPELLANT HAS NOT SHOWN THAT THIS COURT HAS OR SHOULD TAKE JURISDICTION OF THIS CASE UNDER SECTION 128 OF THE JUDICIAL CODE, AMENDED, (28 U.S.C.A. SEC. 225).

Section 128 of the Judicial Code, Amended, (28 U.S.C.A. Sec. 225) provides in part:

“(a) . . . The circuit courts of appeal shall have appellate jurisdiction to review by appeal or writ of error final decisions.

Fourth. In the Supreme Court of the Territory of Hawaii . . . in all civil cases, civil or criminal,

wherein the Constitution or a statute or treaty of the United States or any authority exercised thereunder is involved; . . .”

The appellant did not object in the trial court or in the Supreme Court of the Territory of Hawaii to prosecution's Instruction No. 9, (Record pp. 8-9), on constitutional grounds or on the basis of a statute or treaty of the United States, or any authority exercised thereunder.

The appellant has not based his objection to said instruction in this Court on the ground that a federal question is involved other than to state: “The jurisdiction of this court to review the final judgment of the Supreme Court of the Territory of Hawaii is sustained by Section 128 of the Judicial Code (28 U.S.C.A., Sec. 225).” (Appellant's Brief, p. 2.) The only issue raised by the appellant in this Court is that the trial court erred in giving prosecution's Instruction No. 9, (Record pp. 8-9), by including therein the following nine words: “a doubt that you could give a reason for.” (Appellant's Brief, p. 3.)

(a) Obviously a treaty or statute of the United States or any authority exercised thereunder is not involved herein. The only question is whether or not the Territory's instruction on “reasonable doubt” violates the “due process” clause of the Fifth and

Fourteenth Amendments of the Constitution of the United States.

The Fifth Amendment of the Constitution provides, "... nor be deprived of life, liberty, or property without due process of law; . . ." Const. Am. 1 to 13, U.S.C.A. p. 172.

The Fourteenth Amendment of the Constitution provides, "... nor shall any state deprive any person of life, liberty, or property, without due process of law; . . ." Const. Am. 14 to end, U.S.C.A. p. 69.

(b) The due process clause of the Fifth and Fourteenth Amendments means the same thing except the Fifth Amendment applies to the federal government and its instrumentalities. The Fourteenth Amendment applies to the several states.

The restraints placed on the federal government by the due process clause of the Fifth Amendment in the exercise of legislative power is no greater than those imposed upon the several states by the due process clause of the Fourteenth Amendment.

*Bowles v. Willingham* (1944), 321 U.S. 503,  
64 S. Ct. 641, 88 L. Ed. 892, 905

*Hamilton v. Kentucky Distilleries & W. Co.*  
(1919), 251 U.S. 146, 40 S. Ct. 106, 64 L.  
Ed. 194, 199



*United States v. Darby* (1941), 312 U.S. 100,  
61 S. Ct. 451, 85 L. Ed. 609

In *Hibben v. Smith* (1903), 191 U.S. 310, 24 S. Ct. 88, 48 L. Ed. 195, the Supreme Court of the United States states at *page 201*:

"The 14th Amendment, it has been held, legitimately operates to extend to the citizens and residents of the states the same protection against arbitrary state legislation affecting life, liberty, and property as is offered by the 5th Amendment against similar legislation by Congress; . . ."

The words "due process of law" mean the same in both the Fifth and Fourteenth Amendments. Taylor: Due Process of Law, Sec. 49, p. 107.

In Due Process of Law, *supra*, Taylor, in referring to the words "due process of law" in the Fifth Amendment, states in Section 14, page 23:

"The conclusion is equally irresistible that when the same phrase was employed in the Fourteenth Amendment to restrain the action of the states, it was in the same sense and with no greater extent; . . ."

It therefore follows that decisions involving the due process clause of the Fourteenth Amendment are authority herein.

(c) This case does not involve any federal question but simply a general rule of law.

Even if it were to be assumed *arguendo*, that the trial court committed error in giving Territory's Instruction No. 9 on "reasonable doubt" to the jury by including therein the words, "but a doubt that you could give a reason for," (Record pp. 8-9), it is difficult to see how such error, if any, infringes the personal life and liberty of the defendant in violation of the Fifth and Fourteenth Amendments of the Constitution, or involves a statute or treaty of the United States or any authority exercised thereunder.

When the question of what is a "reasonable doubt" arises, we of the Territory of Hawaii look first to the decisions of the Supreme Court of the Territory of Hawaii and then to the decisions of other jurisdictions because the question appears to us to be essentially one of local and general law rather than one involving a federal question.

In *Kimbrel v. Territory of Hawaii*, (C.C.A. 9th, 1930), 41 Fed. (2d) 740, the Court in dismissing an appeal states at pages 740-741:

"... the question whether the charge contained in the complaint or information is sufficient under the statute is a question of general law, and does not involve either the Constitution or laws of the United States."

Accord: *Barrington v. Missouri* (1907), 205 U.S. 483, 27 S. Ct. 582, 51 L. Ed. 890.

In *The City and County of San Francisco v. Itsell* (1890), 133 U.S. 65, 10 S. Ct. 241, 33 L. Ed. 570, the Supreme Court of the United States states at page 571:

“In the present case, the record of the pleadings, findings of fact and judgment shows that it was unnecessary for that court to decide, and its opinion filed in the case and copied in the record shows that it did not decide, any question against the plaintiff in error, except the issue whether the former judgment rendered against it and in favor of the grantor of the defendants in error was a bar to this action. That was a question of general law only, in no wise depending upon the Constitution, treaties or statutes of the United States.”

In *Giles v. Little* (1890), 134 U.S. 645, 10 S. Ct. 625, 33 L. Ed. 1062, 1063, the Supreme Court dismissed a writ of error for lack of jurisdiction holding that the construction of a will was based on general rules of law and upon local statutes and not on the Constitution, laws or treaties of the United States.

See also:

*City and County of San Francisco v. Jane Scott* (1884), 111 U.S. 768, 4 S. Ct. 688, 28 L. Ed. 593

*United States v. Thompson* (1877), 93 U.S. 586, 23 L. Ed. 982

*Allen v. McVeigh* (1883), 107 U.S. 433, 2 S. Ct. 558, 27 L. Ed. 572

*West v. State of Louisiana* (1904), 194 U.S. 258, 24 S. Ct. 650, 48 L. Ed. 965

(d) The due process clause of the Fifth and Fourteenth Amendments does not prohibit the Territory of Hawaii from enforcing its criminal laws under appropriate statutory provisions and common law doctrines. It does not permit a test by this Court of every ruling made by a territorial court in the course of a trial.

*Buchalter v. New York* (1943), 319 U.S. 427, 63 S. Ct. 1129, 87 L. Ed. 1492, 1495-1496

Taylor: Due Process of Law, Sec. 551, p. 824

(e) Substantial or material error in an instruction to the jury in a criminal case in a court of the Territory of Hawaii does not necessarily violate the due process clause of the Fifth or Fourteenth Amendment.

In *Buchalter v. New York*, *supra*, the Supreme Court of the United States states at pages 1495-1496:

"The due process clause of the Fourteenth Amendment requires that action by a state through any of its agencies must be consistent with the fundamental principles of liberty and justice which lie at the base of our civil and political institutions, which not infrequently are designated as 'the law of the land.' Where this requirement has been disregarded in a criminal trial in a state court this court has not hesitated to exercise its jurisdiction to enforce the constitutional guarantee. But the Amendment does not draw to itself the provisions

of state constitutions or state laws. It leaves the states free to enforce their criminal laws under such statutory provisions and *common law doctrines as they deem appropriate; and does not permit a party to bring to the test of a decision in this court every ruling made in the course of trial in a state court.*" (Emphasis ours.)

Again at page 1496, we find the following:

"... As already stated, the due process clause of the Fourteenth Amendment does not enable us to review errors of state law however material under that law. We are unable to find that the rulings and instructions under attack constituted more than errors as to state law. We cannot say that they were such as to deprive the petitioners of a trial according to the accepted course of legal proceedings."

In *Davis v. State of Texas* (1891), 139 U.S. 651, 11 S. Ct. 675, 35 L. Ed. 300, the Supreme Court of the United States in dismissing the writ of error held that substantial error in an instruction to the jury in a criminal case in a state court does not violate the due process clause of the Fourteenth Amendment.

In "Due Process of Law," by Taylor, Section 551 at page 824, we find the following:

"A substantial error in the charge to the jury in a criminal case in a state court does not deprive the prisoner of the equal protection of the laws or of due process or abridge his immunities, within the Fourteenth Amendment. A writ of error to review the judgment of the highest tribunal of a state



cannot be maintained in the absence of a federal question giving jurisdiction . . .”

(f) The presumption of innocence is as fundamental a concept of our law as the doctrine of reasonable doubt. But failure to instruct on the presumption of innocence has been held not to constitute a denial of due process under the Fourteenth Amendment.

*Howard v. Fleming* (1903), 191 U.S. 126, 24 S. Ct. 49, 48 L. Ed. 121, 125

2. ASSUMING ARGUENDO THAT A FEDERAL QUESTION IS INVOLVED HEREIN, THE WRIT OF ERROR SHOULD BE DISMISSED BECAUSE SUCH FEDERAL QUESTION IS NOT SUBSTANTIAL.

Furthermore, irrespective of the foregoing, this Court has already decided the issue involved herein adversely to the appellant.

*Griggs v. United States*, (C.C.A. 9th), 158 Fed. 572, 577-578

*Louie Ding v. United States*, (C.C.A. 9th), 246 Fed. 80

This appeal is therefore frivolous.

*Equitable Life Ass. Society of the United States v. Brown*, 187 U.S. 308, 311, 23 S. Ct. 123, 47 L. Ed. 190, 192

The appellant's appeal has not presented a substantial federal question.

*Fukunaga v. Territory of Hawaii*, (C.C.A. 9th, 1929), 33 Fed. (2d) 396, 397

*Stanworth v. United States*, (C.C.A. 9th, 1930), 45 Fed. (2d) 158, 159



3. THE CIRCUIT COURT OF THE FIRST JUDICIAL CIRCUIT, TERRITORY OF HAWAII, DID NOT ERR IN GIVING TO THE JURY TERRITORY'S INSTRUCTION NO. 9 ON REASONABLE DOUBT.

The only portion of this entire instruction which the appellant in this Court and in the Supreme Court of the Territory of Hawaii has assigned as reversible error reads: ". . . but a doubt you can give a reason for . . ." (Appellant's Brief, p. 4; Record p. 8.)

(a) The language assigned as error in said instruction has been used by trial courts of Hawaii in their charge to juries on reasonable doubt since 1889.

In *King v. Abop* (1889), 7 Haw. 556, 560-561, the defendant was convicted of murder which was affirmed. The Supreme Court of Hawaii states at page 560:

" . . . the Court charged . . . from notes to *Commonwealth vs. McKie*, 1 Leading Crim. Cases, pages 320-321:

'But if a defendant in a criminal case has a right to have the jury instructed that they must be satisfied of his guilt beyond a reasonable doubt, the question arises, what is a reasonable doubt? It has been defined to be *a doubt for which a reason could be given*. It certainly must be a serious and substantial doubt, not the mere possibility of a doubt . . . ' (Emphasis ours.)

Again at page 561:

"We are of opinion that the jury were rightly instructed by the Court in this charge."

In *Territory of Hawaii v. Robello* (1910), 20 Haw. 7, 22-23, substantially the same instruction on reasonable doubt was given as that complained of herein and it reads as follows:

“The Jury are instructed that the doubt which will entitle defendants or any of them, to an acquittal must be a reasonable doubt, not a conjured-up doubt, such a doubt as you might conjure up to acquit a friend, *but a doubt that you could give a reason for.*

‘A reasonable doubt is not a possible doubt, not a conjectural doubt, not an imaginary doubt, not a doubt of the absolute certainty of the guilt of the accused, because everything relating to human affairs and depending upon moral evidence is open to conjectural or imaginary doubt, and because absolute certainty is not required by law. The real question is whether after hearing the evidence and from the evidence you have or not an abiding belief that defendants are guilty and if you have such belief so formed, it is your duty to convict. You should take all the testimony and all the circumstances into account and act as you have an abiding belief the fact is.’ ” (Emphasis ours.)

The Court at *page 31* held that no error was committed.

The same instruction was before the Supreme Court of the Territory of Hawaii in *Territory of Hawaii v. Buick* (1923), 27 Haw. 28, 36, 40-41, and was again approved.

This instruction has been given in three capital cases that have been before the Territorial Supreme Court for review. (Record pp. 41, 41-42.)

(b) The United States Circuit Court of Appeals for the Ninth Circuit has already settled the issue raised herein adversely to the appellant.

In *Griggs v. United States*, (C.C.A. 9th, 1908), 158 Fed. 572, the plaintiff in error was jointly indicted with another for the crime of obtaining money by false pretenses and was convicted therefor. The Court at pages 577-578 states:

"Counsel for plaintiff in error proffered an instruction on the subject of reasonable doubt. The court declined to instruct as requested, and on that subject instructed the jury as follows:

'The defendant is presumed to be innocent until he is proved guilty by the evidence before you beyond a reasonable doubt. By reasonable doubt is not meant any doubt or conjecture which may occur to your mind, or may be imagined by you; *but it is a doubt which must arise from the evidence, or lack of evidence, and for which some reason can be given.*'

Error is assigned both to the refusal to charge as requested and to the charge as given; but the only question to be determined here is whether there is reversible error in the instruction which was given. In *Owens v. United States*, 130 Fed. 283, 64 C.C.A. 529, in reversing the judgment of the trial court for error in a certain instruction,

this court thought it proper to suggest that the following definition of 'reasonable doubt,' given to the jury by the court below, should be omitted on a new trial:

'A reasonable ground of doubt is one which is reasonable from the evidence or want of evidence. It must be a ground of doubt *for which a reason can be given*, which reason must be based upon the evidence or want of evidence.'

And this court remarked:

'A doubt arising out of evidence is a mental operation for which it may often be very difficult, and indeed impossible, to assign any reason, and yet, if honestly entertained by the jury in a criminal case, must be acted upon; for they are only authorized to bring in a verdict of guilty when satisfied and convinced beyond a reasonable doubt of the guilt of the accused. Such a doubt has been often and correctly defined as a doubt which is reasonable in view of all of the evidence, and such as arises upon an impartial comparison and consideration of all of it, and prevents the jury from being able candidly and truthfully to say that they have an abiding conviction of the defendant's guilt.'

It will be observed that this court, while disapproving the phraseology of the instruction, carefully refrained from expressing the opinion that it was ground for reversing the judgment then under consideration. In the definitions of 'reasonable doubt' there is hopeless confusion in the adjudicated cases. Definitions approved in some courts have been reversible error in others. The difficulty lies in explaining words which perhaps define themselves better than can be done by any paraphrase or eluci-

dition. Said Mr. Justice Woods in *Miles v. United States*, 103 U.S. 312, 26 L. Ed. 481:

'Attempts to explain the term "reasonable doubt" do not usually result in making it any clearer to the minds of the jury.'

The definition which was given by the court below in the present case was given in substance by Chief Justice Waite in *United States v. Butler*, 1 Hughes (U.S.) 457, Fed. Cas. No. 14,700, and has been sustained in a number of cases, and, among others, in the following federal decisions: *United States v. Stevens*, 2 Hask. (U.S.) 164, Fed. Cas. No. 16,392; *United States v. Johnson* (C.C.) 26 Fed. 682; *United States v. Jackson* (C.C.) 29 Fed. 503; *United States v. Jones* (C.C.) 31 Fed. 718; *United States v. Cassidy* (D.C.) 67 Fed. 782. The objection to that definition lies in the danger of conveying the impression to the jurors that the reason for the doubt must be one that can be expressed in words. For this reason it has been rejected in a number of jurisdictions. In others, with better reason, we think, it has been disapproved, but held not to constitute reversible error. *State v. Sauer*, 38 Minn. 438, 38 N.W. 355; *People v. Stubenvoll*, 62 Mich. 329, 28 N.W. 883; *State v. Morey*, 25 Or. 241, 35 Pac. 655, 36 Pac. 573. And we so hold in the present case." (Emphasis ours.)

The *Griggs case*, *supra*, carefully limited the legal effect of the comments in *Owens v. United States*, (C.C.A. 9th, 1904), 130 Fed. 279, 283, on a similar instruction of reasonable doubt, which were in the nature of obiter dicta, by definitely holding that the



giving of such an instruction did not constitute reversible error.

In *Louie Ding v. United States*, (C.C.A. 9th, Rehearing denied), 246 Fed. 80, Louie Ding and Louie Lung Gin together with others were indicted and convicted for the crime of conspiracy. At page 83, the Court states:

“In defining a ‘reasonable doubt’ the court charged as follows:

‘Now, a “reasonable doubt” is just such a doubt which you can give a reason. When a juror is convinced to a moral certainty of the truth of the fact, then he is convinced beyond a reasonable doubt. It is not a doubt which is imaginary, conjectural, or speculative. Sometimes we say a reasonable doubt is such a doubt as a reasonable person in determining an issue of like concern to himself as that before the jury to the defendant would make him pause or hesitate in arriving at his conclusions.’

Defendants object to the declaration that a reasonable doubt is such a doubt as the jury are able to give a reason for. We concede that the phraseology objected to is not a clear explanation, but when it is considered in connection with the whole instruction there was no reversible error. This court so held in *Griggs v. United States*, 158 Fed. 572, 85 C.C.A. 596, and similar ruling was made by the Court of Appeals for the Second Circuit in *Marshall v. United States*, 197 Fed. 511, 117 C.C.A. 65.” (Emphasis ours.)

The language objected to in both the Ding case and the case at bar is almost identical and the Court



held that when the whole instruction was considered there was no reversible error.

(c) Territory's Instruction No. 9 considered and construed in toto is not erroneous.

In *Mansfield v. United States*, (C.C.A. 8th, 1935), 76 Fed. (2d) 224, the appellants were indicted and convicted of using the mails and of conspiracy to use the mails to defraud. The Court states at page 230:

"It is contended that the court erred in defining reasonable doubt as a doubt for which a reason could be assigned. Although no proper exception was taken preserving the question for review [*McCutchan v. United States* (C.C.A. 8) 70 F. (2d) 658; *Stassi v. United States* (C.C.A. 8) 50 F. (2d) 526], we are satisfied that no prejudice resulted from the form and substance of the instruction, which was as follows:

"These underlying principles are that the law presumes the innocence and not the guilt of the accused. This presumption attends and protects them and each of them until the Government has overcome such presumption by testimony which may satisfy you of their guilt beyond a reasonable doubt.

By reasonable doubt I do not mean the mere fanciful, flimsy, fictitious notion that the defendants or either of them might be innocent but I mean, as the word implies, a doubt founded in reason *and a doubt for which you could give a reason*. It means a substantial doubt arising on the testimony or from lack of testimony, and such a

doubt as would cause you as reasonable men to halt and to hesitate before you acted in the more serious matters of your own concerns.'

An instruction in almost identical language was approved by the Supreme Court in *Hopt v. Utah*, 120 U.S. 430, 7 S. Ct. 614, 30 L. Ed. 708. See, also, *Wilson v. United States*, 232 U.S. 563, 34 S. Ct. 347, 58 L. Ed. 728; *United States v. Woods* (C.C.A. 2) 66 F. (2d) 262; *Murphy v. United States* (C.C.A. 3) 33 F. (2d) 896; *Colbeck v. United States* (C.C.A. 8) 14 F. (2d) 801, 803; *Estabrook v. United States* (C.C.A. 8) 28 F. (2d) 150; *Pettine v. Territory of New Mexico* (C.C.A. 8) 201 F. 489; *Dunbar v. United States*, 156 U.S. 185, 15 S. Ct. 325, 39 L. Ed. 390; *Sotello v. United States* (C.C.A. 5) 256 F. 721; *Maupin v. United States* (C.C.A. 4) 258 F. 607.

In *Colbeck v. United States*, *supra*, this court said: 'It is also contended that there should be a reversal because the court erred in its instruction to the jury on the subject of reasonable doubt. The particular respect in which it is claimed the court erred on that subject is that it charged the jury that a reasonable doubt is a doubt based on reason and which is reasonable in view of all the evidence. If the court had stopped there the contention would be a serious one. But that was not all of the instruction. Taking the court's entire charge on that subject it is the same in substance as the instruction given in *Hopt v. Utah*, 120 U.S. 430, 7 S. Ct. 614, 30 L. Ed. 708, which the Supreme Court held did not constitute reversible error.'

The part of the instruction complained of was qualified and explained by the sentence immediately

following: 'Such doubt as would cause you as reasonable men to halt and to hesitate before you acted in the more serious matters of your own concerns.' The instruction informs the jury that it was their duty to acquit if the evidence left them with such a doubt of guilt as a reasonable man would decline to act upon his own affairs. *Sotello v. United States, supra.*" (Emphasis ours.)

In the *Mansfield case, supra*, the phrase used is "a doubt for which you could give a reason," while in the case at bar the phrase used is, ". . . a doubt that you could give a reason for." (Record p. 8.) And the Court held that the inclusion of the above phrase was not error. This case is from the same circuit as *Pettine v. Territory of New Mexico*, (C.C.A. 8th, 1912), 201 Fed. 489, and *Ayer v. Territory of New Mexico*, (C.C.A. 8th, 1912), 201 Fed. 497, cited by appellant on pages 5-7, and 7 respectively of his brief in support of his contention that the phrase contained in the instruction under consideration constituted reversible error.

(d) The appellant's criticism herein is "hyper-critical."

In *Marshall v. United States*, (C.C.A. 2nd, 1912), 197 Fed. 511; Certiorari denied, 226 U.S. 207, 33 S. Ct. 112, 57 L. Ed. 379, the appellant was convicted of using the mails to defraud, and appealed. The case

was reversed on other grounds but the Court held that an instruction on reasonable doubt did not constitute error and stated at *pages 512-513*:

“There was no error in charging the jury that ‘by the term reasonable doubt is meant not a capricious doubt, *but a substantial doubt—a doubt that you can give a reason for if the court called on you to give one.*’ The definition of ‘reasonable doubt’ as being a doubt for which a reason can be given is frequently adopted by trial judges. The criticism that the charge carried with it an implied threat that the jury might be called upon to explain to the court the reason which induced them to acquit if they found a verdict of not guilty, is hypercritical.” (Emphasis ours.)

(e) The language complained of herein or similar language has been used and upheld by a large number of federal courts.

In *United States v. Woods*, (C.C.A. 2nd, 1933), 66 Fed. (2d) 262, the appellants and others were indicted and convicted of conspiracy. The Court states at *page 265*:

“The court charged that a reasonable doubt was one *for which a reason could be assigned*. While we do not approve such a definition, it has in this circuit been held not to be erroneous . . .” (Emphasis ours.)

In *Murphy v. United States*, (C.C.A. 3rd, 1929), 33 Fed. (2d) 896; Certiorari denied, 280 U.S. 584, 50 S. Ct. 35, 74 L. Ed. 634, the appellant was con-

victed of unlawfully importing merchandise into the United States. During the trial the Court gave the following instruction on reasonable doubt, at page 896, *footnote 1*:

“ ‘The burden of proof is on the Government to establish their guilt, and the burden of proof is on the Government to establish their guilt beyond a reasonable doubt.

“Reasonable doubt” are words hardly requiring to be defined. You know what “reasonable doubt” is. It is not incumbent upon the Government to prove the guilt of these men beyond all doubt, because very few human affairs can be shown to exist beyond all possible doubt. “*Reasonable doubt*” means a doubt for which some sound reason can be assigned in your minds. It does not mean a doubt which may be conjured up, as sometimes is done, for the purpose of avoiding an unpleasant duty. One court has said it is an honest, conscientious misgiving generated by truth, or the want of it; such a state of proof as fails to convince your judgment, your conscience and to satisfy your reason of the guilt of the accused. That is about all there is to that.’ ” (Emphasis ours.)

The sole error assigned in *Murphy v. United States*, *supra*, was the emphasized portion of the instruction set out above. The Court held this was not error.

The portion of the instruction complained of in the case at bar is designed to enable each juror to distinguish in his own mind a reasonable doubt from a



“conjured up” doubt as in *Murphy v. United States*, *supra*, or to distinguish a “reasonable doubt” from “a slight doubt” . . . “a probable doubt . . . a possible doubt . . . a conjectural doubt . . . an imaginary doubt.” (Record pp. 8-9.) It does not mean that he must give such reason to the court or to his fellow jurymen or to anyone. It simply provides each juror with a yardstick that he can use in determining whether or not the government has sustained the burden of proof required by law. Neither the burden of proof nor quantum of proof is changed in any respect.

In *Sotello v. United States*, (C.C.A. 5th, 1919) 256 Fed. 721, the appellant was indicted and convicted of transporting munitions of war for export. The Court state at pages 723-724:

“It is assigned as error that the court, in charging the jury upon the question of reasonable doubt, said *that a reasonable doubt must be a doubt for which a sensible man could give a good reason*, which reason must be based upon the evidence or the want of evidence. The following is the part of the court’s charge which dealt with the subject of reasonable doubt:

‘The defendant in this case is presumed to be innocent until his guilt is established by legal and competent evidence beyond a reasonable doubt, and if you have a reasonable doubt of his guilt you



should acquit him. By reasonable doubt you will understand that the court does not mean fanciful conjecture which an imaginative man may conjure up, but the doubt which reasonably flows from the evidence, or the want of evidence, and a doubt for which the sensible man could give a good reason, which reason must be based on the evidence, or the want of evidence, such a doubt as a sensible man would act upon or decline to act upon in his own concerns. If you have such a doubt, the defendant is entitled to the benefit of that doubt and you should acquit him; but if you are satisfied from the evidence that he is shown to have committed the offense with which he is charged, you should find him guilty.'

The part of the instruction of which complaint is made was qualified and explained by the language which immediately followed it, forming a part of the same sentence—'*such a doubt as a sensible man would act upon or decline to act upon in his own concerns.*' The instruction as a whole was such as to make it known to the jury that it was their duty to acquit the defendant, if the evidence left them with such a doubt of his guilt as a sensible man would act upon or decline to act upon in his own concerns. *The instruction as a whole was such that the defendant could not have been prejudiced by it. Hopt v. Utah*, 120 U.S. 430, 7 Sup. Ct. 614, 30 L. Ed. 708.

Of other rulings complained of no more need be said than that no one of them constituted reversible error." (Emphasis ours.)

In the *Sotello case*, *supra*, the Court held that the language objected to in the instruction was explained

by the language that followed it and that was sufficient. The same principle applies to the case at bar. The language preceding and following the phrase, "but a doubt that you could give a reason for" (Record pp. 8-9), fully explains it. The language used in the second paragraph of the instruction contains the heart of the classic definition of "reasonable doubt" given by Chief Justice Shaw in *Commonwealth v. Webster*, 5 Cush. (Mass.) 295, at page 320, 52 Am. Dec. 711, at 731.

In *Colbeck v. United States*, (C.C.A. 7th, 1925), 10 Fed. (2d) 401, 404; Certiorari denied, *Colbeck v. United States*, 271 U.S. 662, 46 S. Ct. 474, 70 L. Ed. 1138, the Court held that it was not error to give an instruction on reasonable doubt which contained the following: ". . . A reasonable doubt, gentlemen, is just such a doubt as the name implies—a doubt based upon reason, . . ."

Chief Justice Waite in charging the jury on reasonable doubt in *United States v. Butler*, (Circuit Court D. So. Carolina, 1877), Cas. No. 14,700, 1 Hughes 457, 25 Fed. Cas. 213 at page 226, stated: ". . . It must be a doubt for which a reason may be assigned . . ."

Accord: *United States v. Stevens*, (Circuit Court D. Maine, 1877), Cas. No. 16,392, 2 Hask. 164, 27 Fed. Cas. 1312 at page 1314.

In *United States v. Johnson*, (Circuit Court, S.D. Georgia, 1885), 26 Fed. 682, 685, Judge Speer in charging the jury on "reasonable doubt" included the phrase: "... a doubt for which a good reason, arising from the evidence, can be given . . ."

Accord: *United States v. Jackson*, (Circuit Court S.D. Georgia, 1886), 29 Fed. 503.

Judge Morrow in *United States v. Cassidy*, (District Court N.D. California, 1895), 67 Fed. 698, included in his charge to the jury on reasonable doubt at page 782, the phrase: "a doubt for which a good reason can be given, . . ."

Judge Sater in *United States v. Guthrie*, (District Court S.D. Ohio E.D., 1909), 171 Fed. 528 at page 532, included in his charge to the jury on reasonable doubt the words: "... not a mere possible, or conjured up, or imaginary doubt, but one for which you can give a reason, . . ."

In *United States v. Wilson*, (Circuit Court S.D. Florida, 1910), 176 Fed. 806, at page 809, the Court in charging the jury on reasonable doubt, stated: "A reasonable doubt does not mean every doubt that may

flit through your minds in the consideration of this case, *but a doubt for which you can give a reason if called on to do so.*" (Emphasis ours.)

In *United States v. Hill*, (District Court D. Maryland, 1924), 1 Fed. (2d) 954, at page 956, the Court charged the jury on "reasonable doubt" as follows:

"... The burden of proof is on the United States to satisfy the jury of his guilt. And the jury must be satisfied beyond a reasonable doubt, before they are authorized to find a verdict of guilty. To be convinced beyond a reasonable doubt is to have an abiding conviction to a moral certainty of the guilt of the accused. Such a doubt as would justify the acquittal of the defendant *must be a doubt for which you can give a reason.*" (Emphasis ours.)

In *United States v. Sussman*, (District Court E.D. Penn., 1941), 37 Fed. Supp. 294, the defendants moved for a new trial including as one of their grounds therefor, that the court committed error in giving that portion of the charge on reasonable doubt set out on page 296, which reads: "... '*The term reasonable doubt means a doubt for which a good reason can be given in the light of all the evidence.*'" (Emphasis ours.) This was overruled on the basis that considering the charge as a whole the jury was not misled and the defendants were not "wronged."

In *Maupin v. United States*, (C.C.A. 4th, 1919), 258 Fed. 607, the conviction of the plaintiff in error was affirmed with the Court stating:

"... The case is brought here on the narrowest technical ground. On the subject of reasonable doubt and the presumption of innocence, the following instruction was given to the jury:

'Where a defendant is placed on trial charged with an offense, the law presumes that he is innocent, and it devolves on the government to prove every material fact necessary to constitute the offense charged against him to the satisfaction of the jury beyond a reasonable doubt, and if the government has failed to do that then it is the duty of the jury to acquit the defendant.'

This covers the subject fully, and it is of no consequence that the instruction was not in the language requested by counsel . . ."

The instruction upheld in the *Maupin case*, *supra*, does not even attempt to define "reasonable doubt" and it was held sufficient.

(f) The instructions given by the trial court on the presumption of innocence, burden of proof and reasonable doubt fully protected the appellant.

The jury was repeatedly admonished by the court that the burden of proof was on the Territory and that the defendant was presumed to be innocent and could not be convicted until the Territory had proven



him guilty beyond a reasonable doubt. (Territory's Instruction No. 9.) (Record pp. 8-9.)

**"TERRITORY'S INSTRUCTION NO. 11**

"You are instructed that the *burden is on the Territory to prove beyond a reasonable doubt* that the defendant's treatment of Rose Dolim was not for the purpose of saving her life." (Record p. 9.) (Emphasis ours.)

**"DEFENDANT'S INSTRUCTION NO. 2**

"I instruct you that the issue which you are to try is that presented by the indictment, and the defendant's plea of not guilty in this case. For be it remembered that the plea of not guilty puts in issue and requires the *prosecution to prove each and every material allegation in the indictment beyond all reasonable doubt.*" (Record p. 10.) (Emphasis ours.)

**"DEFENDANT'S INSTRUCTION NO. 3**

"The indictment in this case is a mere accusation and is not of itself any evidence, not the slightest, of the defendant's guilt, and no juror should permit himself to be to any extent influenced because or on account of the indictment against the defendant. *You are instructed that the defendant is presumed by the law to be innocent of the crime charged against him, in each and all its parts, and this presumption shields and protects him throughout each and every stage of the trial until overcome by satisfactory evidence, which convinces you of his guilt as charged beyond all reasonable doubt.*" (Record pp. 10-11.) (Emphasis ours.)



**"DEFENDANT'S INSTRUCTION NO. 4**

"Moreover, I instruct you that this presumption of innocence is not a mere form to be disregarded by you at pleasure, but it is an essential, substantial part of the law of the land, and is binding upon you in this case, and it is your duty to give the defendant the full benefit of this presumption and to acquit him unless, as I have already stated, the evidence satisfies you of his guilt beyond all reasonable doubt." (Record p. 11.)

**"DEFENDANT'S INSTRUCTION NO. 7**

"Under the law no jury can convict a person charged with crime upon mere suspicion, however strong, or simply because there is a preponderance of all the evidence in the case against him, or simply because there are strong reasons to suspect him guilty. What the law requires before a person can be convicted of crime is not suspicion, not mere probabilities, *but proof which excludes all reasonable doubt of his innocence.*" (Record p. 12.) (Emphasis ours.)

Territory's Instruction No. 9 (Record pp. 8-9), did not change the burden or quantum of proof. It still left "reasonable doubt" as reasonable doubt.

(g) The term "reasonable doubt" is self-defining. Territory's Instruction No. 9 could not therefore be prejudicial.

In *United States v. Breen*, (C.C.A. 2d, 1938) 96 Fed. (2d) 782, the Court states at *page* 784:

"... The simple fact is that the term 'reasonable doubt' is so largely self-defining that attempts to use language from which the jury will get a clearer understanding of what it means than the words themselves convey may often be futile. And, because that is so, an attempted explanation which leaves reasonable doubt at the end still reasonable doubt, cannot be prejudicial . . ."

(h) The language used, considering the entire instruction, was favorable to the appellant and "is sustained by respectable authority."

The same can be said for Territory's Instruction No. 9 (Record pp. 8-9), as was said in *Miles v. United States* (1881), 103 U.S. 304, 312, 26 L. Ed. 481, at page 484, where Mr. Justice Woods speaking for the Court states:

"The charge of the court defining what is meant by the phrase 'reasonable doubt' is assigned as ground of error.

The evidence upon which a jury is justified in returning a verdict of guilty must be sufficient to produce a conviction of guilt, to the exclusion of all reasonable doubt. Attempts to explain the term 'reasonable doubt' do not usually result in making it any clearer to the minds of the jury. The language used in this case, however, was certainly very favorable to the accused and is sustained by respectable authority. *Com. v. Webster*, 5 Cush. 320; *Arnold v. State*, 23 Ind., 170; *State v. Nash*, 7 Iowa 347; *State v. Ostrander*, 18 Iowa 435; *Don-*

*nelly v. State*, 2 Dutch., 601; *Winter v. State*, 20 Ala. 39; *Giles v. State*, 6 Ga. 276.

We think there was no error in the charge, of which the plaintiff in error can justly complain . . .”

Accord:

*Dunbar v. United States* (1895), 156 U.S. 185,  
15 S. Ct. 325, 39 L. Ed. 390, 395

The federal courts with the exception of two cases cited by the appellant from the United States Circuit Court of Appeals for the Eighth Circuit, hold that an instruction defining reasonable doubt which includes the phrase: “but a doubt that you could give a reason for,” or words of similar import do not constitute a basis for reversing the judgment of conviction of trial courts.

(i) The state courts are not as uniform as the federal courts in upholding instructions containing substantially the same language as that objected to herein, but the majority rule follows the federal cases cited herein.

The decisions of the state courts may readily be classified as they were by the Supreme Court of the Territory of Hawaii in its opinion in this case, viz: “In some jurisdictions similar instructions have been sustained. In others they were held to constitute prejudicial error. And in still others, though criticized, the

error, if any, was considered harmless." (Record pp. 39-40.)

In *Butler v. State* (1899), 102 Wis. 364, 78 N.W. 590, the plaintiff in error was convicted of murder, and on appeal, objected to the trial court's use in its charge defining reasonable doubt, of the words "a doubt for which a reason can be given." The Wisconsin court in overruling this objection states at *page* 592:

" . . . The phrase assailed is not an incorrect method of stating the distinction between that measure of uncertainty which justifies an acquittal and the mere fanciful, unfounded speculative doubt which can always be raised, even as to the existence of facts most obvious to our senses. A doubt cannot be reasonable unless a reason therefor exists, and, if such reason exists, it can be given."

In *Emery v. State* (1899), 101 Wis. 627, 78 N.W. 145, at pages 152-155, an instruction containing similar language was upheld. The Court stated at *page* 153:

" . . . Most persons of wide experience as trial judges have been impressed very strongly, and on many occasions, that the due administration of justice requires a careful explanation to the jury of the meaning of the important legal term here discussed, to the end that they shall not act on the theory that mere impression or surmise that the accused may be innocent, or is possibly innocent, will justify an acquittal even though they be convinced of guilt by the evidence produced in court, with such degree of certainty as to leave in their

minds, as men of ordinary common sense and experience in life, no reasonable theory consistent with innocence. That such a situation *is quite liable to be met with and justice defeated*, the efficacy of law to protect society doubted, and its administration by the courts discredited, is quite plain to persons, generally, who have presided at criminal trials and met with such painful experiences. In the judgment of the writer a careful explanation of the term 'beyond a reasonable doubt' should be given to all juries in criminal cases, and especially in important trials. The jury should be so carefully instructed to minimize the danger of their mistaking the language 'beyond a reasonable doubt' to mean beyond a mere doubt or mere possibility of innocence, or a doubt other than one founded on or arising out of, or for the want of, evidence produced in court; that it means what the language, broadly considered, naturally signifies, *that is, beyond any doubt founded in reason and common sense as applied to the evidence. They should be made to understand that if they arrive at the degree of certainty indicated by the explanation given, a conviction should follow notwithstanding there may yet remain in their minds some mere doubt, or doubt not founded in reason, . . .*" (Emphasis ours.)

The Supreme Court of Kansas after carefully considering the adjudicated cases of the various federal and state courts held in *State v. Patton* (1903), 66 Kan. 486, 71 Pac. 840, that the words "'Such a doubt as the jury are able to give a reason for,'" did not constitute error in an instruction similar to the



one in the present case. The Court stated at pages 840-841:

"The instruction given should be considered as an entirety. By so doing it is observable that in elucidation of the expression 'reasonable doubt' the requirement of a reason for doubt is set over against capriciousness, conjecture, the indulgence of speculation upon possibilities, and the invasion of the realm of imagination. Instructions presenting such a contrast have been approved in the following cases: *Hodge v. The State*, 97 Ala. 37, 12 South. 164, 38 Am. St. Rep. 145; *Vann v. The State*, 83 Ga. 44, 9 S.E.945; *State v. Jefferson*, 43 La. Ann. 995, 10 South. 199; *The People v. Guidici*, 100 N.Y. 503, 3 N.E. 493; *State v. Harras* (Wash.) 65 Pac. 774; *Wallace v. State*, 41 Fla. 547, 26 South. 713; *Butler v. State*, 102 Wis. 364, 78 N.W. 590; *State v. Rounds*, 76 Me. 123; *State v. Serenson*, 7 S.D. 277, 64 N.W. 130."

The Court at page 841 states:

"The theory of the instruction is tersely and accurately put in *Butler v. State*, where it is said:

"The phrase assailed is not an incorrect method of stating the distinction between that measure of uncertainty which justifies an acquittal and the mere fanciful, unfounded, speculative doubt which can always be raised, even as to the existence of *facts most obvious to our senses*. *A doubt cannot be reasonable unless a reason therefor exists, and, if such reason exists, it can be given.*" (Emphasis ours.)

Accord:

*State v. Fox*, 116 Kan. 180, 225 Pac. 1042



In *People v. Guidici*, 100 N.Y. 503, 3 N.E. 493, the defendant was convicted of murder in the first degree, and on appeal, Guidici contended that the portion of the instruction on reasonable doubt which defined it as being "a doubt for which some good reason arising from the evidence can be given" was reversible error. In order that the comments of the court in affirming the judgment of convicted error be fully understood it is necessary to set forth a portion of the instruction, page 495, viz:

"... You must understand what a reasonable doubt is. It is not a mere guess or surmise that the man may not be guilty. It is such a doubt as a reasonable man might entertain after a fair review and consideration of the evidence,—a doubt for which some good reason arising from the evidence can be given . . ."

The New York Court states at *page 495*:

"... The criticism is limited to the definition given of a reasonable doubt, and aimed at that portion where, by way of paraphrase, the trial judge said, 'a doubt for which some good reason arising from the evidence can be given.' It should be read with the whole sentence of which it forms a part, and, so taken, seems only to distinguish that doubt which would avail the prisoner from one which is merely vague and imaginary."

Again at *pages 495-496*, the Court states:

"... We find in the language of the judge nothing to mislead or perplex a juror; but if counsel

at the trial thought otherwise, the attention of the court should have been directed to it. 'An indefinable doubt, which cannot be stated, with the reason upon which it rests, so that it may be examined and discussed, can hardly be considered a reasonable doubt, as such an one would render the administration of justice impracticable; and, as to this, it has not been too strongly said, "All the authorities agree."' Note to section 29, 3 Greenl. Ev. (14th Ed.)."

In *People v. Lagroppo*, 90 App. Div. 219, 86 N.Y.S. 116, 126, the defendant was convicted of murder in the second degree. The New York Court in affirming the judgment held that an instruction on reasonable doubt which contained the following: "... 'A reasonable doubt is such a doubt as a man of reasonable intelligence can give some good reason for entertaining if he is called upon to do so . . .'" was not error.

In *State v. Serenson*, 7 S.D. 277, 64 N.W. 130, 132, the defendant was convicted of embezzlement, and on appeal, contended that a portion of the instruction on reasonable doubt containing the following was error: "A reasonable doubt is a doubt which has some reason for its basis. It does not mean a doubt from mere caprice or groundless conjecture. A reasonable doubt is such a doubt as the jury are able to give a

reason for." The South Dakota Court held that this did not constitute error, and at *page 132* stated:

"... The able law writer Austin Abbott, in his Brief for Criminal Cases, at *page 487*, discusses a 'reasonable doubt,' and says: 'The gist of the rule is that the law contemplates a doubt for which a good reason, arising on the evidence, can be given, ...'"

In *State v. Grant*, 20 S.D. 164, 105 N.W. 97, the same Court states at *page 99*:

"Concerning reasonable doubt, the court charged the jury as follows: 'The term "reasonable doubt" is pretty well understood, but not easily defined. It is not the mere possibility of a doubt, not an imaginary doubt, not a doubt of the absolute certainty of the guilt of the defendant, because everything relating to human affairs and depending upon moral evidence is open to some conjectural or imaginary doubt, and because absolute certainty is not required by the law. It is not such a doubt as one might conjure or hatch up in order to acquit a friend, without any reason therefor; but it must be a substantial doubt, and one which would ordinarily impress the judgment of a prudent man in the graver and more important affairs of life. The reasonable doubt which entitles defendant in a criminal case to an acquittal is a doubt of guilt, reasonably arising from all the evidence in the case, *and it must be such a doubt as the juror is able to give a reason for.* A reasonable doubt is that state of a case which, after the entire comparison and consideration of all the evidence, leaves the mind of the juror in that condition that he

cannot say and feel an abiding conviction to a moral certainty of the guilt of the defendant as charged in the information.'

The italicized clause is claimed to be misleading, prejudicial, and erroneous. Substantially the same phrase has been sustained in a number of cases; in others, it has been regarded as erroneous; while in others, it has been disapproved, though not held to be reversible error. 23 Am. & Eng. Ency. Law (2d) Ed. 960. Such having been the condition of the case law on the subject, this court was at liberty to adopt the view deemed most consonant with sound reason, when it held that such an instruction, qualified substantially as it was in the case at bar, did not justify a reversal. *State v. Serenson*, 7 S.D. 277, 65 N.W. 130. Further research and reflection having served to strengthen confidence in the conclusion then announced, we are constrained to hold that the charge in this case, taken as a whole should be sustained." (Emphasis ours.)

The foregoing instruction taken as a whole is substantially the same as that given in the case at bar.

In *State v. Sonnenschein* (1916), 37 S.D. 585, 159 N.W. 101, 106, the Court held that an instruction on reasonable doubt which contained the following: ". . . it must be such a doubt as the juror is able to give a reason for," was not erroneous.

In *State v. Merry* (1939), 136 Me. 243, 8 Atl. (2d) 143, the appellant was convicted of murder, and appealed. The Maine Court states at page 153:

"As the term is used in instructing juries in criminal cases, a reasonable doubt is not a vague, fanciful or speculative doubt, but a doubt arising out of the case as presented, *for which some good reason may be given*, and such a doubt as, in the graver transactions of life, would cause reasonable, fair-minded, honest and impartial men to hesitate and pause. 8 R.C.L. 220, *State v. Reed*, 62 Me. 129, 143." (Emphasis ours.)

In *State v. Butler*, 148 S.C. 495, 146 S.E. 418, the appellant objected to the use by the trial court in its charge on reasonable doubt, of the phrase "for which doubt you can give a sound and substantial reason." The South Carolina Court in overruling the objection states at *page 419*:

"... 'All of these words are used, not in the sense of powerful, or overwhelming, but simply in contradiction to the words "flimsy," "fanciful," or "slight," and we cannot suppose that a jury would ever understand them in any other way. The law does not require that a criminal charge shall be proved beyond the slightest doubt, and it is only where the evidence leaves upon the minds of the jury—not a weak or slight doubt—but a serious or strong and well-founded doubt as to the truth of the charge, that the law, in its mercy, declares that the accused shall have the benefit of the doubt.'

Under the rule as laid down in the Bodie Case, we do not see any error in the charge of the presiding judge in this case."

In *Bryant v. State*, 197 Ga. 641, 30 S.E. (2d) 259, the defendant was convicted of murder and sen-



tenced to electrocution. On appeal the conviction was affirmed. The Georgia Court states at *page* 269:

“Ground 26 of the amended motion complains of error in the charge of the court on the subject of reasonable doubt, to wit: ‘Now a reasonable doubt is just what the term implies. It is a doubt based upon reason, *a doubt for which you can give a reason,*’ the particular objection being to the phrase, ‘*a doubt for which you can give a reason.*’ This exact language has heretofore been held not to be error. *Vann v. State*, 83 Ga. 44 (4), 9 S.E. 945; *Jordan v. State*, 130 Ga. 406 (1), 60 S.E. 1063; *Arnold v. State*, 131 Ga. 494 (4), 62 S.E. 806; *Hudson v. State*, 153 Ga. 695 (12), 113 S.E. 519; *Holmes v. State*, 194 Ga. 849 (2), 22 S.E. 2d 808; *Andrews v. State*, 196 Ga. 84 (10), 26 S.E. 2d 263.

Counsel’s motion to reconsider and overrule these cases is denied.” (Emphasis ours.)

In *State v. Jefferson*, 43 La. Ann. 995, 10 So. 199, 200, the defendant was indicted for murder and was convicted of manslaughter. The Louisiana Court in affirming the judgment of the lower court held that the inclusion of the words, “‘. . . It is a serious, sensible doubt such as you could give a good reason for, . . .’” in an instruction defining reasonable doubt was not error.

In *King v. State* (1920), 17 Ala. App. 536, 87 So. 701, 702-703, the defendant was convicted of manslaughter. The Alabama Court held that the inclusion



of the words, "' . . . it is a doubt for which a reason can be given' " in an instruction defining reasonable doubt was not error.

In *Wallace v. State*, 41 Fla. 547, 26 So. 713, 723-725, the Florida Court reversed the judgment because of error in the sentence but after analyzing and discussing the cases both for and against held that an instruction on reasonable doubt which includes the words: "' . . . That 'a "reasonable doubt" is a doubt for which you can give a reason; . . . ' " was not error, stating at pages 724-725:

" . . . We are of opinion that the instruction complained of does no more than to state, in a different form, the same thing as that defined in other language in the Lovett and Woodruff Cases. It tells the jury that the burden is upon the state to establish defendant's guilt beyond a reasonable doubt,—that is, beyond a doubt for which they can give an intelligent reason; that this doubt may arise either from affirmative evidence tending to show innocence, or from lack of evidence sufficient to establish guilt; but that, if the evidence of guilt satisfies them to such an extent as to leave them without a doubt that defendant may be innocent for which they can give an intelligent reason, they should convict. This instruction puts no burden upon the defendant to furnish the jury with a reason, but it requires the state to satisfy the jury of defendant's guilt to such an extent as to leave their minds without a doubt that defendant may be innocent for which they can give an intelligent

reason. Of course, the jury are not required to state reasons for their verdict, but they are nevertheless required, by the law and by their duties as jurors, to act in the jury box as reasonable beings, and to exercise their reasoning faculties in passing upon the life and liberty of accused persons. If they entertain a doubt, they must, as reasonable men, know upon what that doubt is based, and they are required to examine into the nature and origin of the doubt far enough to ascertain that it is a reasonable one. And, if it be found that no intelligent reason can be given for entertaining a doubt, how can the conscience of the jury be satisfied with a verdict of acquittal, resting, as it does, under a solemn duty to convict, where the evidence convinces them of guilt to that extent as to leave no reasonable doubt upon their minds? To authorize an acquittal because of some vague, undefined, unintelligible, or inexplicable misgiving is to eliminate the word 'reasonable' from the definition."

In *State v. Dunn*, 159 Wash. 608, 294 Pac. 217, the Washington Court states at pages 218-219:

"Neither is there merit in the contention that an instruction by the court was not an adequate and complete explanation of reasonable doubt. That the term 'reasonable doubt' is clearly, though concisely, explained, is patent from a reading of the instruction, which is as follows:

'The expression "beyond a reasonable doubt" has been used by me a number of times in these instructions, and judges sometimes instruct juries at great length about its meaning. *It simply means that the proof must be beyond a doubt for which the juror who entertains the doubt can assign a*

*good reason.* If any juror has a doubt as to the guilt of the defendant, for which doubt he can assign a good reason, it will be the duty of that juror to vote not guilty, but if there is no such doubt, then it will be the duty of the juror to vote guilty.' ” (Emphasis ours.)

In *People v. Grove*, 284 Ill. 429, 120 N.E. 277, the Illinois Court states at page 281:

“The seventh instruction is objected to because it requires that *a doubt must be one that the jury can give a reason for and not a conjured-up doubt, and it is contended that one may have a reasonable doubt for which he can give no reason.* While it is questionable whether instructions defining reasonable doubt add anything to the meaning of the words themselves, the instruction is not wrong.” (Emphasis ours.)

In *State v. Gilbert*, 8 Idaho 346, 69 Pac. 62, 63-64, the defendant was convicted of murder in the second degree. The Idaho Court held that an instruction on reasonable doubt including the following language: “. . . A reasonable doubt is . . . a doubt which a juryman can give a reason for . . .” was not erroneous.

In *State v. Morey*, 25 Ore. 241, 36 Pac. 573, 577-578, on rehearing, the Supreme Court of Oregon after attempting to analyze the various cases on the subject held that an instruction on reasonable doubt containing the words, “. . . A reasonable doubt is such a

doubt as a juror can give a reason for . . .” was not reversible error and stated at *page 578*:

“ . . . The particular language in question may be, and no doubt is, subject to the criticism that it does not define, but needs defining; but we do not think it could have misled or perplexed the jury when considered in connection with the remainder of the instruction. *If every criminal case is to be reversed for some technical inaccuracy in the definition of a ‘reasonable doubt,’ then, indeed, the ‘administration of justice becomes impracticable.’* Fully realizing the consequences of this decision, we have given the questions presented the utmost care, and, finding no error in the record, have no alternative but to adhere to our former opinion.” (Emphasis ours.)

In *People v. Steubenvoll*, 62 Mich. 329, 28 N.W. 883, 884, 885, the Michigan Court criticized the use of the phrase, “. . . which you can give some good reason,” in an instruction on reasonable doubt but held that it did not constitute reversible error.

Accord: *State v. Sauer*, 38 Minn. 438, 38 N.W. 355.

In *People v. Yun Kee*, 8 Cal. A. 82, 96 Pac. 95, the defendant objected to an instruction on reasonable doubt including the language: “. . . A reasonable doubt is a doubt based upon reason, and growing out of the testimony and evidence in the case . . .” The

California Court in holding this was not error states at page 96:

"... If a reasonable doubt growing out of the evidence in the case is not to be based upon reason, we are at a loss to discover a foundation for it, unless it be based upon mere conjecture and irrational speculation, and this is not permissible."

The appellant (Peter L. Young) in the case at bar cites as an authority, *Pettine v. Territory of New Mexico*, 201 Fed. 489, (Appellant's Brief, pages 5-7) and *Ayer v. Territory of New Mexico*, 201 Fed. 497, (Appellant's Brief, page 7), both from the Eighth Circuit Court of Appeals, but the case of *Mansfield v. United States*, 76 Fed. (2d) 224, 230, from the same circuit clearly indicates that neither the Pettine nor the Ayer case applies to the case at bar.

The appellant likewise cites *Cowan v. State*, 22 Neb. 519, (Appellant's Brief, page 7); *State v. Parks*, 96 N.J. Law 360, 115 Atl. 305, (Appellant's Brief, pages 7-8); *State v. Rosenberg*, 97 N.J. Law 430, 118 Atl. 207, (Appellant's Brief, pages 8-9), and *State v. Linker*, 94 N.J. Law 412, 111 Atl. 35, (Appellant's Brief, page 9), which do support his contention. These cases do not represent the weight of authority as stated in Appellant's Brief, page 9, but represent the minority view. The great weight of authority as



shown by the cases cited herein supports the decision of the Supreme Court of the Territory of Hawaii.

Quoting from *page 208 of State v. Rosenberg, supra*, cited by the appellant (Appellant's Brief, pages 8-9), we find the following:

"... We have adopted the doctrine of reasonable doubt as defined by Chief Justice Shaw, in *Commonwealth v. Webster*, 5 Cush. (Mass.) 295, at page 320, 52 Am. Dec. 711, in *Donnelly v. State*, 26 N.J. Law, 601, 26 page 615. The test there furnished as to when a reasonable doubt may be properly said to have arisen is stated as follows:

'Reasonable doubt is not a mere possible doubt. It is that state of the case which, after the entire comparison and consideration of all the evidence, leaves the minds of the jurors in that condition that they cannot say they feel an abiding conviction to a moral certainty of the truth of the charge.' "

This is the test furnished by Chief Justice Shaw in *Commonwealth v. Webster*, 5 Cush. (Mass.) 295, 320, 52 Am. Dec. 711, and is essentially the test furnished in Territory's Instruction No. 9. (Record pages 8-9.) The last sentence reads: "... The real question is whether after hearing the evidence and from the evidence you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty and if you have such belief so formed,



it is your duty to convict and if you have not such belief so formed it is your duty to acquit."

The Supreme Court of the Territory of Hawaii stated: "... These instructions have taken the form of a definition of the adjective 'reasonable,' the inclusion of instruction of what are not reasonable doubts and the time-honored test enunciated by Chief Justice Shaw in *Commonwealth v. Webster* reported in 5 Cush. (Mass.) 295, 320." (Record page 41.)

The instruction in controversy is of this type. The instruction does not change the burden of proof. The instruction does not require any juror to give to any one his reasons for voting either for conviction or otherwise. But it does give him positive and negative guides that better enable him to judge whether or not his doubts, if any, are reasonable.

A reasonable doubt is one based on reason, if based on reason the juror can give it to himself or to his fellow jurymen during his deliberation. On the other hand, if it is not based on reason then it may be a "conjured-up doubt," or a "slight doubt," or a "probable doubt," or a "possible doubt," or a "conjectural doubt," or "an imaginary doubt." (Record p. 8.)

The instruction given by the Territory does not place upon the defendant the burden to develop reasonable doubt in the evidence.

## CONCLUSION

It is respectfully submitted that the appellant has not shown that this Court has or should take jurisdiction of this case under *Section 128 of the Judicial Code, Amended*, (28 U.S.C.A. Sec. 225).

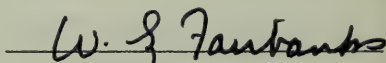
Furthermore, irrespective of the foregoing, this Court has already decided the issue herein adversely to the appellant and the appeal is therefore frivolous.

Finally, the trial court did not err in giving the jury Territory's Instruction No. 9 on reasonable doubt.

The error assigned therefore is without merit and the judgment appealed from should be affirmed.

Dated at Honolulu, T. H., this 17 day of April, A. D. 1946.

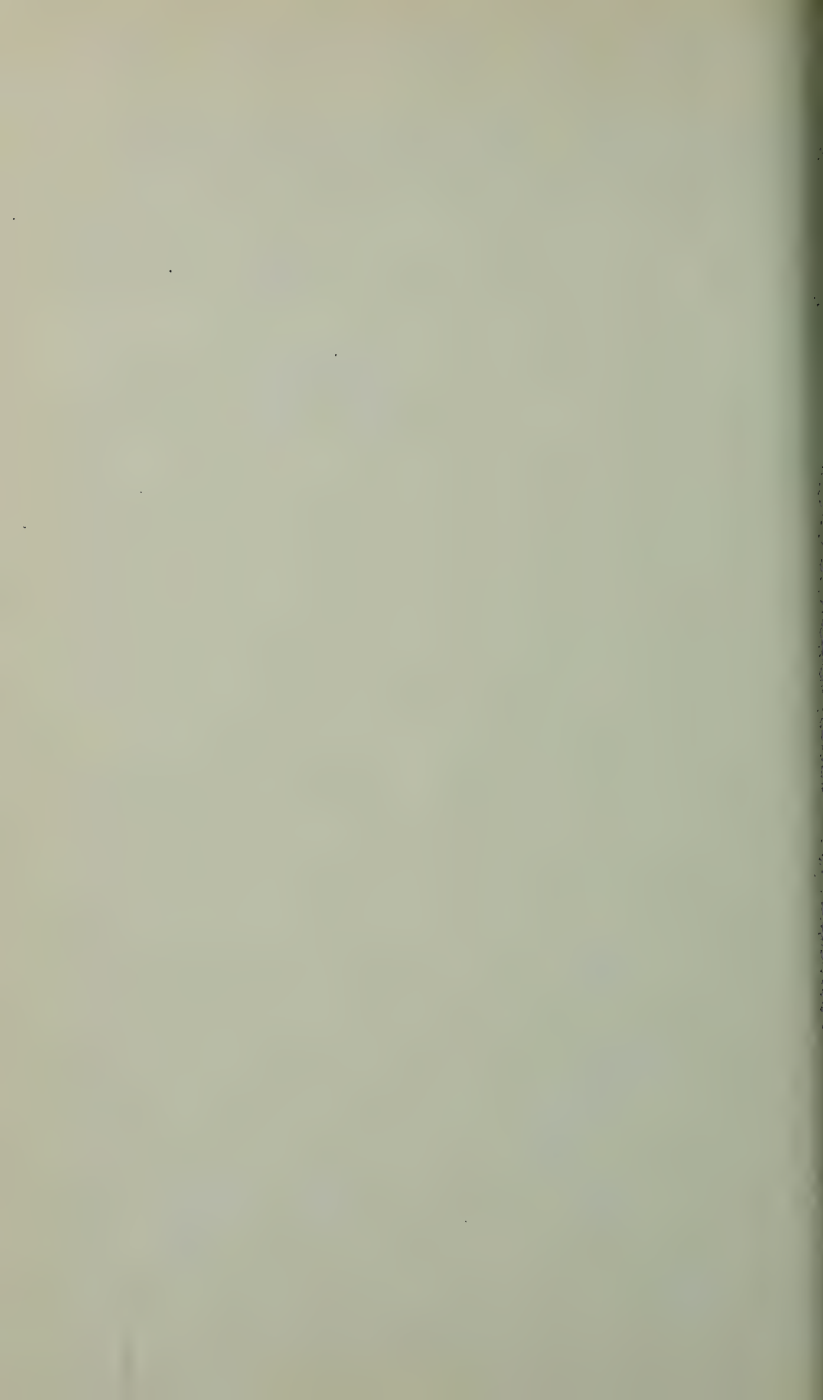
Respectfully submitted,

  
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Receipt of three copies of the foregoing brief is acknowledged this 17<sup>th</sup> day of April, A.D. 1946.

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No. 11,144

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

---

PETER L. YOUNG,

*Appellant,*

VS.

TERRITORY OF HAWAII,

*Appellee.*

SUPPLEMENTAL BRIEF FOR APPELLANT.

---

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FILED

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No. 11,144

IN THE

# United States Circuit Court of Appeals

For the Ninth Circuit

---

PETER L. YOUNG,

*Appellant,*

VS.

TERRITORY OF HAWAII,

*Appellee.*

---

## SUPPLEMENTAL BRIEF FOR APPELLANT.

---

### FOREWORD.

At the oral argument, appellant was granted permission to file a supplemental brief discussing (1) the jurisdiction of this court to entertain the appeal, and (2) the decisions of this court respecting reasonable doubt in criminal cases.

---

1. THE JURISDICTION OF THIS COURT TO REVIEW THE FINAL JUDGMENT OF THE SUPREME COURT OF THE TERRITORY OF HAWAII IS SUSTAINED BY SECTION 128 OF THE JUDICIAL CODE (28 U.S.C.A., SEC. 225).

The pertinent parts of the section provide:

“(a) \* \* \*. The circuit courts of appeals shall have appellate jurisdiction to review by appeal or writ of error final decisions— \* \* \*

Fourth. In the Supreme Courts of the Territory of Hawaii \* \* \*, in all civil cases, civil or criminal, wherein the Constitution or a statute or treaty of the United States or any authority exercised thereunder is involved; \* \* \*.”

The constitutional guaranties of the Federal Bill of Rights are applicable to the Territory of Hawaii.

*Duncan v. Kahanamoku*, 66 S.Ct. 606, 613.

*Waialua Agr. Co. v. Christian*, 305 U.S. 91, 109,  
59 S.Ct. 21, 30, 88 L. Ed. 60.

*Farrington v. Tokushige*, 273 U.S. 284, 298, 299,  
47 S.Ct. 406, 409, 71 L.Ed. 646.

*Lovato v. New Mexico*, 242 U.S. 199, 37 S.Ct.  
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*Rasmussen v. United States*, 197 U.S. 516, 25  
S.Ct. 514, 49 L.Ed. 862.

*Hawaii v. Mankichi*, 190 U.S. 197, 23 S.Ct. 787,  
47 L.Ed. 1016.

*Callan v. Wilson*, 127 U.S. 556, 8 S.Ct. 1301, 32  
L.Ed. 223.

Therefore, this court has jurisdiction to review the final decision of the Supreme Court of the Territory of Hawaii to determine if appellant was denied “due process of law” under the Federal Bill of Rights.

*Farrington v. Tokushige*, 273 U.S. 284, 298, 299,  
47 S.Ct. 406, 409, 71 L.Ed. 646.

*Lovato v. New Mexico*, 242 U.S. 199, 37 S.Ct.  
107, 108, 61 L.Ed. 244.



Questions of "due process of law" are not to be treated "narrowly or pedantically, in slavery to forms or phrases".

*Pearson v. McGraw*, 308 U.S. 313, 318, 60 S.Ct. 211, 213, 84 L.Ed. 293.

*Burnett v. Wells*, 289 U.S. 677, 678, 53 S.Ct. 761, 764, 77 L.Ed. 1439.

"As applied to a criminal trial, denial of due process is the failure to observe that fundamental fairness essential to the very concept of justice."

*Lisenba v. California*, 314 U.S. 219, 236, 62 S.Ct. 280, 290, 86 L.Ed. 166.

"'Due process of law' contemplates a trial in a criminal case by a fair jury with full evidence and correct instructions as to the law".

*Henderson v. State*, Fla., 20 So. 2d 659, 661.

In criminal cases, "due process of law" contemplates proper instructions on reasonable doubt.

*Howard v. Fleming*, 191 U.S. 176, 24 S.Ct. 49, 50, 51, 48 L.Ed. 121.

In criminal cases, "due process of law" is denied by instructions which set at naught the established principles of reasonable doubt.

*Howard v. Fleming*, 191 U.S. 176, 24 S.Ct. 49, 50, 51, 48 L.Ed. 121.

*Chaffee v. United States*, 85 U.S. 516, 545, 21 L.Ed. 909, 914.

*Paddock v. United States*, 9 Cir. 1935, 79 F. 2d 872, 877.

As the case was decided in a territorial court and appellant is maintaining that he was denied rights based upon the Federal Bill of Rights, the jurisdiction of this court to entertain the appeal is not open to doubt.

Turning to another aspect of section 128 of the Judicial Code, counsel for appellant have been unable to find any construction of the words "or any authority exercised thereunder" appearing in said section. Somewhat similar language was considered and construed by the Supreme Court in *Milligar v. Hartuppee*, 73 U.S. 258, 261, 18 L.Ed. 829, 830, decided in 1868, but the case is of no practical help.

The Supreme Court of the Territory of Hawaii exercises its authority under section 81 of the Hawaiian Organic Act. (48 U.S.C.A., sec. 63.) In the exercise of that authority its decisions must be in conformity with the Constitution of the United States. (*Waialua Agr. Co. v. Christian*, 305 U.S. 91, 109, 59 S.Ct. 21, 30, 81 L.Ed. 60.) It cannot deprive an individual of his Constitutional protections by an application of territorial law. (*Duncan v. Kahanamoku*, 66 S.Ct. 606, 613.) In the present case, and in the exercise of its authority under the said Organic Act of Hawaii, the territorial Supreme Court applied the territorial law respecting instructions on reasonable doubt. (T. 41-42.) Appellant's position is that the territorial Supreme Court thereby denied him "due process of law". The present case therefore involves the exercise of authority by the Supreme Court of the Territory of Hawaii, under the Organic Act of

Hawaii, whereby it is claimed by appellant his rights under the Federal Bill of Rights were violated. On this aspect, the jurisdiction of this court to entertain the appeal would also seem clear.

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## 2. THE DECISIONS OF THIS COURT RESPECTING REASONABLE DOUBT IN CRIMINAL CASES.

The instruction challenged on this appeal reads in its entirety as follows (T. 8-9), the italics indicating the portion around which the controversy revolves on the appeal:

“I further instruct you that the burden of proof is upon the Territory and the law presumes the defendant to be innocent, and this presumption continues and attends him at every stage of the case until it has been overcome by evidence which proved him guilty to your satisfaction and beyond a reasonable doubt. And in this connection, I instruct you that the doubt which will entitle the defendant to an acquittal must be a reasonable doubt, not a conjured-up doubt, such a doubt as you might conjure up to acquit a friend, *but a doubt that you could give a reason for.*

A reasonable doubt is not a slight doubt, not a probable doubt, not a possible doubt, not a conjectural doubt, not an imaginary doubt, not a doubt of the absolute certainty of the guilt of the accused, because everything relating to human affairs and depending upon mortal (moral) evidence is open to conjectural or imaginary doubt, and because absolute certainty is not required by law. The real question is whether after hearing

the evidence and from the evidence you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty and if you have such belief so formed, it is your duty to convict and if you have not such belief so formed it is your duty to acquit.”

The subject of reasonable doubt has been considered by this court on many occasions. Without purporting to exhaust the list, the following may be cited:

*Rose v. United States*, 1945, 149 F. 2d 755, 759.

*Henderson v. United States*, 1944, 143 F. 2d 681, 682.

*Pon Wing Quong v. United States*, 1940, 111 F. 2d 751, 757.

*Paddock v. United States*, 1935, 79 F. 2d 872, 876, 877.

*De Groot v. United States*, 1935, 78 F. 2d 244, 251, 252.

*Kearns v. United States*, 1928, 27 F. 2d 854, 855.

*Arine v. United States*, 1926, 10 F. 2d 778, 780, 781.

*Dell 'Aira v. United States*, 1926, 10 F. 2d 102, 106.

*Raffour v. United States*, 1922, 284 F. 720, 721.

*McCurry v. United States*, 1922, 281 F. 532, 533.

*Crane v. United States*, 1919, 259 F. 480, 483, 484.

*Louie Ding v. United States*, 1917, 246 F. 80, 83.

*Sheppard v. United States*, 1916, 236 F. 73, 80.  
*Griggs v. United States*, 1908, 158 F. 572, 577,  
 578.

*Owens v. United States*, 1904, 130 F. 279, 283.

In three of the cited cases the court considered instructions containing language similar to that italicized in the instruction prefacing this subdivision. The first case was *Owens v. United States*, 130 F. 279, where the instruction was as follows (p. 283): "A reasonable ground of doubt is one which is reasonable from the evidence or want of evidence. *It must be a ground of doubt for which a reason can be given, which reason must be based upon the evidence or want of evidence*". (Emphasis added.) In disapproving the language thus emphasized, the court said (p. 283):

"A doubt arising out of evidence is a mental operation for which it may often be very difficult, and, indeed, impossible, to assign any reason, and yet, if honestly entertained by the jury in a criminal case, must be acted upon, for they are only authorized to bring in a verdict of guilty when satisfied and convinced beyond a reasonable doubt of the guilt of the accused."

The second case was *Griggs v. United States*, 158 F. 572, where the instruction was as follows (p. 577): "The defendant is presumed to be innocent until he is proved guilty by the evidence before you beyond a reasonable doubt. By reasonable doubt is not meant any doubt or conjecture which may occur to your mind, or may be imagined; *but it is a doubt which must arise from the evidence or lack of evidence, and*



*for which some reason can be given*". (Emphasis added.) Again the court disapproved the language emphasized, but did not regard it as constituting reversible error in the particular case. A dissenting opinion by the judge who wrote the opinion in the *Owens* case (p. 578) was committed to the view that the instruction constituted reversible error.

And the third case was *Louie Ding v. United States*, 246 F. 80, where the instruction was as follows (p. 83): "*Now a 'reasonable doubt' is just such a doubt for which you can give a reason. When a juror is convinced to a moral certainty of the truth of the fact, then he is convinced beyond a reasonable doubt. It is not a doubt which is imaginary, conjectural, or speculative. Sometimes we say a reasonable doubt is such a doubt as a reasonable person in determining an issue of like concern to himself as that before the jury to the defendant would make him pause or hesitate in arriving at his conclusions*". (Emphasis added.) Once more, the court disapproved the language emphasized but did not regard it as constituting reversible error in the particular case.

In none of the three cases mentioned was the jury told, as it was told in this case (T. 8), that "A reasonable doubt is \* \* \* not a probable doubt". The question in this particular case, therefore, is not only whether the language emphasized in the challenged instruction constitutes reversible error, but also whether that language constitutes reversible error in view of the setting in which it is found.



Five of the cited cases consider the question of "probable doubt". (*Rose v. United States*, 1945, 149 F. 2d 755, 759; *Henderson v. United States*, 143 F. 2d 681, 682; *Pon Wing Quong v. United States*, 1940, 111 F. 2d 751, 757; *Kearns v. United States*, 1928, 27 F. 2d 854, 855; *Arine v. United States*, 1926, 10 F. 2d 778, 780, 781.)

In *Rose v. United States*, 149 F. 2d 755, it was said, at page 759:

"It should be remembered too, that: 'The proof in a criminal case need not exclude all doubt. If that were the rule, crime would be punished only by the criminal's own conscience, and organized society would be without defense against the conscienceless criminal and against the weak, the cowardly and the lazy who would seek to live on their wits. The proof need go no further than reach that degree of probability where the general experience of men suggests that it has passed the mark of reasonable doubt.' *Henderson v. United States*, 9 Cir. 1944, 143 F. 2d 681, 682."

In *Pon Wing Quong v. United States*, 111 F. 2d 751, it was said, at page 757:

"Appellant thinks the following statement as found in one of the instructions constitutes error: 'You are to consider the strong probabilities of the case'. His argument is that 'The jury must of necessity construe such language to the effect that they were entitled under the law in determining the guilt or innocence of the appellant *to speculate* as to whether or no the appellant was guilty \* \* \*.' (Italics supplied.)

Such argument fades out when the next line of the instruction is read: 'A conviction is justified only when such probabilities exclude all reasonable doubt as the same has been explained to you.' "

In *Kearns v. United States*, 27 F. 2d 854, it was said, at page 855:

"Counsel earnestly insists that the instruction defining a reasonable doubt was condemned by this court in *Arine v. United States*, 10 F. 2d 778, but such is not the case. The only definition of reasonable doubt found in that case was, 'A persistent judgment to a very high degree of probability that the defendant is guilty as charged,' while here the instruction goes far beyond that. In fact, the instructions in the two cases have little in common, aside from the use of the expression, 'a persistent judgment to a very high degree of probability,' found in each. Here the court instructed the jury at length that there was a reasonable doubt, unless from the evidence the jury formed and had an abiding conviction to a moral certainty that the defendants were guilty, that an abiding conviction is a persistent judgment, and that you can confidently act upon it in the gravest affairs of life; that in any case proof can only be made to some degree of probability, but in a criminal case the proof of guilt must be that very high degree of probability that inspires a persistent judgment that the defendant is guilty as charged; that such high degree of probability must be based upon facts and circumstances in evidence, and not at all upon conjectures, speculation, or the doctrine of chances; that, if the

jury had an abiding conviction, that is to say, a persistent judgment to a moral certainty, that the defendants were guilty as charged, they had no reasonable doubt and should convict accordingly; that the jury might have doubt of the guilt of the defendant, but it would nevertheless be their duty to convict unless their judgment approved such doubt as a reasonable one. It will thus be seen that the court defined a reasonable doubt in different ways, many of which, at least, have met with universal approval. The court treated the different definitions given as synonymous, and whether they were or not we need not inquire, because we are convinced that the jury was not and could not be mislead."

And in *Arine v. United States*, 10 F. 2d 778, it was said, at pages 780 and 781:

"In defining reasonable doubt the court said: 'If you have a persistent judgment to a very high degree of probability that the defendant is guilty as charged, you have no reasonable doubt, and you are bound to convict him.' A number of courts have held that conviction beyond a reasonable doubt means more than a conclusion that there is a very high probability of guilt. \* \* \* We think the court erred in his definition of reasonable doubt. For this and the other errors pointed out, the judgment is reversed, and the cause remanded for a new trial."

These quotations make it obvious that a "reasonable doubt" justifying an acquittal in a criminal action may be a "probable doubt". The language emphasized in the challenged instruction—language

which this court has consistently disapproved—therefore appears in a setting surcharged with error. Manifestly, the situation here is quite different from that disapproved but tolerated in the *Griggs* and *Louie Ding* cases.

It must be noted, moreover, that the *Griggs* case was decided in 1908 and the *Louie Ding* case in 1917. Later decisions of this court have been more solicitous in protecting the rights of defendants in criminal actions against erroneous instructions on the vital element of reasonable doubt. This is illustrated by the reversals of the judgments in *Arine v. United States*, 1926, 10 F. 2d 778, *De Groot v. United States*, 1935, 78 F. 2d 244, and *Paddock v. United States*, 1935, 79 F. 2d 872. Equal solicitousness on the same vital element would indicate that the passive disapproval in the *Griggs* and *Louie Ding* cases be converted into active disapproval and a conclusion of reversible error.

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### CONCLUSION.

Appellant again respectfully submits that the judgment appealed from should be reversed.

Dated, San Francisco, California,  
September 30, 1946.

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HERBERT CHAMBERLIN,

*Attorneys for Appellant.*

No. 11144

IN THE

# United States Circuit Court of Appeals

For The Ninth Circuit

---

PETER L. YOUNG,  
*Appellant,*

vs.

TERRITORY OF HAWAII,  
*Appellee.*

Upon Appeal from the Supreme Court of the Territory of Hawaii

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ANSWER TO SUPPLEMENTAL BRIEF FOR APPELLANT

FILED

DEC 11 1904

PAUL P. UNDERHILL,

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of the City and County of Honolulu,  
Territory of Hawaii  
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No. 11144

IN THE

# United States Circuit Court of Appeals

For The Ninth Circuit

PETER L. YOUNG,

*Appellant,*

vs.

TERRITORY OF HAWAII,

*Appellee.*

## ANSWER TO SUPPLEMENTAL BRIEF FOR APPELLANT

### INTRODUCTION

At the oral argument held in this Court, August 30, 1946, the appellant was granted permission to file a Supplemental Brief on (1) the jurisdiction of this Court to entertain the appeal, and (2) the subject of reasonable doubt. The Territory was granted permission to file a reply to the Supplemental Brief for Appellant.

### ARGUMENT

1. **THE APPELLANT HAS NOT SHOWN THAT THIS COURT HAS OR SHOULD TAKE JURISDICTION OF THIS CASE UNDER SECTION 128 OF THE JUDICIAL CODE, AMENDED, (28 U.S.C.A. SEC. 225).**

*Section 128 of the Judicial Code, Amended, (28 U.S.C.A. Sec. 225)* provides in part:

“(a) . . . The circuit courts of appeal shall have appellate jurisdiction to review by appeal or writ of error final decisions—

Fourth. In the Supreme Courts of the Territory of Hawaii . . ., in all civil cases, civil or criminal, wherein the Constitution or a statute or treaty of the United States or any authority exercised thereunder is involved; in all other civil cases wherein the value in controversy, exclusive of interest and costs, exceeds \$5,000, and in all habeas corpus proceedings.”

There is no question that the constitutional guarantees of the federal Bill of Rights are applicable to the Territory of Hawaii including the “due process” clause of the Fifth Amendment. (Territory’s Answering Brief, pp. 11-12; Supplemental Brief for Appellant, p. 2.)

(a) **THIS CASE DOES NOT INVOLVE THE “DUE PROCESS” CLAUSE OF THE FIFTH AMENDMENT TO THE CONSTITUTION OR ANY FEDERAL QUESTION.**

We pointed out in Territory’s Answering Brief, pages 12-13, that the “due process” clause of the Fifth and Fourteenth Amendments mean the same thing except the Fifth Amendment applies to the federal government and its instrumentalities while the Fourteenth Amendment applies to the several states.

Material error in an instruction to the jury in a criminal case in a territorial court does not violate the “due process” clause of the Fifth Amendment.

*Buchalter v. New York* (1943), 319 U.S. 427, 63 S. Ct. 1129, 87 L. Ed. 1492, 1495-1496. (cited on pp. 16-17, Territory's Answering Brief.)

*Davis v. State of Texas* (1891), 139 U.S. 651, 11 S. Ct. 675, 35 L. Ed. 300. (cited on page 17, Territory's Answering Brief.)

"*Due Process of Law*" by Taylor, Section 551, p. 824. (cited on pp. 17-18, Territory's Answering Brief.)

In *Buchalter v. New York* (1843), *supra*, the Supreme Court of the United States defines "due process" and the law applicable herein at pages 1495-1496:

"The due process clause of the Fourteenth Amendment requires that action by a state through any of its agencies must be consistent with the fundamental principles of liberty and justice which lie at the base of our civil and political institutions, which not infrequently are designated as 'the law of the land.' Where this requirement has been disregarded in a criminal trial in a state court this court has not hesitated to exercise its jurisdiction to enforce the constitutional guarantee. But the Amendment does not draw to itself the provisions of state constitutions or state laws. It leaves the states free to enforce their criminal laws under such statutory provisions and *common law doctrines as they deem appropriate; and does not permit a party to bring to the test of a decision in this court every ruling made in the course of a trial in a state court.*" (Emphasis ours.)

Again at *page 1496*, we find the following:

" . . . As already stated, the due process clause of the Fourteenth Amendment does not enable us to review errors of state law however material under that law. We are unable to find that the rulings and instructions under attack constituted *more than errors as to state law*. We cannot say that they were such as to deprive the petitioners of a trial according to the accepted course of legal proceedings." (Emphasis ours.)

In *Walker v. Sauvinet*, 92 U.S. 90, 23 L. Ed. 678, the Court states at *page 679*:

"The States, so far as this Amendment is concerned, are left to regulate trials in their own courts in their own way. A trial by jury in suits at common law pending in the State Courts is not, therefore, a privilege or immunity of national citizenship, which the States are forbidden by the Fourteenth Amendment to abridge. A State cannot deprive a person of his property without due process of law; but this does not necessarily imply that all trials in the state courts affecting the property of persons must be by jury. This requirement of the Constitution is met, if the trial is had according to the settled course of judicial proceedings."

In *Collins v. Johnston*, 237 U. S. 502, 35 S. Ct. 649, 59 L. Ed. 1071 at 1077-1078, the Court states:

" . . . He contends that he was deprived of due process of law, in violation of the 14th Amendment, in that the trial court arbitrarily denied and refused to consider a valid and legally conclusive defense offered by him upon the trial of the second indict-



ment, which resulted in the conviction upon which he is now held in custody. . . .

Nor are we able to see that the refusal of the proffered defense, even were such refusal erroneous, could at all affect the jurisdiction of the court, or amount to more than an error committed in the exercise of jurisdiction."

In *Frank v. Mangum*, 237 U.S. 309, 35 S. Ct. 582, 59 L. Ed. 969, the Court states at *page* 979:

"As to the 'due process of law' that is required by the 14th Amendment, it is perfectly well settled that a criminal prosecution in the courts of a state, based upon a law not in itself repugnant to the Federal Constitution, and conducted according to the settled course of judicial proceedings as established by the law of the state, so long as it includes notice and a hearing, or an opportunity to be heard, before a court of competent jurisdiction, according to established modes of procedure, is 'due process' in the constitutional sense." (citing authorities.)

Again the Court states in reference to "due process" at *page* 983:

". . . This familiar phrase does not mean that the operations of the state government shall be conducted without error or fault in any particular case, nor that the Federal courts may substitute their judgment for that of the state courts, or exercise any general review over their proceedings, but only that the fundamental rights of the prisoner shall not be taken from him arbitrarily or without the right to be heard according to the usual course of law in such cases."

Again at page 986:

"... In adopting it, the state declares in effect, as it reasonably may declare, that the right of the accused to be present at the reception of the verdict is but an incident of the right of trial by jury; *and since the state may, without infringing the 14th Amendment, abolish trial by jury, it may limit the effect to be given to an error respecting one of the incidents of such trial.*" (Emphasis ours.)

In *Caldwell v. Texas*, 137 U.S. 692, 11 S. Ct. 224, 34 L. Ed. 816, the Court states at 818:

"By the Fourteenth Amendment the powers of the States in dealing with crime within their borders are not limited, but no State can deprive particular persons or classes of persons of equal and impartial justice under the law. Law, in its regular course of administration through courts of justice, is due process, and when secured by the law of the State, the constitutional requisition is satisfied. 2 Kent Com. 13. And due process is so secured by laws operating on all alike, and not subjecting the individual to the arbitrary exercise of the powers of government, unrestrained by the established principles of private right and distributive justice. *Bank of Columbia v. Okely*, 17 U.S. 4 Wheat. 235, 244. . . . The power of the State must be exerted within the limits of those principles, and its exertion cannot be sustained when special, partial and arbitrary. *Hurtado v. California*, 110 U.S. 516, 535. . . . No question of repugnancy to the Federal Constitution can be fairly said to arise when the inquiry of the state courts is directed to the sufficiency of an indictment in the ordinary administration of criminal law, and the statutes authorizing the form

of indictment pursued are not obviously violative of the fundamental principles above adverted to."

In *Leeper v. State of Texas*, 139 U.S. 462, 11 S. Ct. 577, 35 L. Ed. 225, at page 227, the Court states:

"The sufficiency of the indictment, the degree of the offense charged, the admissibility of the testimony objected to and the alleged disqualification of the juror because he was not a freeholder were all matters with the disposition of which, as exhibited by this record, we have nothing to do."

(b) **THE "CONSTITUTION OR A STATUTE OR TREATY OF THE UNITED STATES OR ANY AUTHORITY EXERCISED THEREUNDER" WAS NOT "INVOLVED" IN THIS CASE.**

In order that a federal question be "involved" as required by *Section 128 of the Judicial Code, Amended*, (28 U.S.C.A. Sec. 225), herein, such question must be presented in either the trial court or the Supreme Court of the Territory of Hawaii. The first time such question was raised was in this Court.

In *Brown v. Missouri K. & T. Ry. Co.*, 175 Mo. 185, 74 S.W. 973, the Supreme Court of Missouri states at page 974:

"But in order that the case can involve a constitutional question, the protection of the Constitution must be timely and properly invoked in the trial court, and that protection must have been denied to the party invoking it by that court, and such party must have been the losing party in the trial court, and proper exceptions saved to the ruling of the trial court. (citing authorities.) The

constitutional protection must be properly invoked in the trial court. It cannot be invoked for the first time in an appellate court. (citing authorities.)

Unless the constitutionality of an act under which the proceeding is had is expressly challenged in the trial court, and the challenge overruled by the trial court, and exception saved in that court, and unless the challenging party is the losing party in the lower court, the appeal will lie to the Court of Appeals, and not to this court, and the Court of Appeals must decide the case without any regard whatever to the constitutional question, for in such a state of the record there is no constitutional question involved in the case. If neither party raises a constitutional question, then the case will be decided by the appellate court that has jurisdiction of the appeal on other grounds, the same as if it had not been possible to raise a constitutional question. *In short, a constitutional question must be raised before it can be involved, and, if it is not involved, then the decision of the case can decide no such question.*" (Emphasis ours.)

See also: *Moore v. Missouri*, 159 U.S. 673, 679-680, 16 S. Ct. 179, 40 L. Ed. 301.

- (c) **THE PHRASE "OR ANY AUTHORITY EXERCISED THERE-UNDER IS INVOLVED" USED IN SECTION 128 OF THE JUDICIAL CODE, AMENDED, (28 U.S.C.A. SEC. 225), DOES NOT INCLUDE ALL QUESTIONS DECIDED BY THE SUPREME COURT OF THE TERRITORY BECAUSE SAID COURT EXISTS BY VIRTUE OF AN ACT OF CONGRESS, TO WIT: SECTION 81 OF THE ORGANIC ACT OF THE TERRITORY (48 U.S.C.A. SEC. 631).**

If the foregoing were not true then Congress would not have deemed it necessary to expressly provide for appeals in criminal cases "wherein the Constitution or

a statute or treaty of the United States or any authority exercised thereunder is involved.” (28 U.S.C.A. Sec. 225.)

Our territorial Supreme Court might render a decision contrary to the “due-process clause” under the Bill of Rights but if that question had not been expressly raised by the appellant in the Supreme Court of the Territory the right to appeal would not exist as pointed out in Point 1 (b) in pages 7 to 8 of this memorandum. Neither the *Waiialua Agricultural Company v. Christian*, 305 U.S. 91, 109, 59 S. Ct. 21, 83 L. Ed. 60, nor *Duncan v. Kahanamoku*, 324, U.S. 833, 66 S. Ct. 606, 631, 89 L. Ed. 1398, cited in Supplemental Brief for Appellant, page 4, applies to the facts presented in the case at bar.

*Brown v. Missouri K. & T. Ry. Co.*, *supra*, 175 Mo. 185, 74 S.W. 973, 974.

*Moore v. Missouri*, *supra*, 159 U.S. 673, 679-680, 16 S. Ct. 179, 40 L. Ed. 301.

Assuming *arguendo* that the appellant was denied “due process of law” by the decision of the Supreme Court of the Territory of Hawaii in this case would not in and of itself give this Court jurisdiction. The two cases of *Farrington v. Tokushige*, 273 U.S. 284, 298, 299, 47 S. Ct. 406, 71 L. Ed. 646, and *Lovato v. New Mexico*, 24 U.S. 199, 37 S. Ct. 107, 61 L. Ed.



244, cited on page 2 of Supplemental Brief for Appellant to the effect that if the decision of the territorial Supreme Court denied "due process" that would give this court jurisdiction, do not so hold. In the *Lovato case*, the Court states at page 247:

"As the case was tried in a territorial court, the denial of asserted rights based upon the 5th and 6th Amendments presents questions within our jurisdiction."

The language in the *Lovato case* must be construed in the light of the facts presented there, and of the two "asserted rights" therein mentioned. One was expressly raised in the trial court and the other in the state supreme court but both were based on constitutional grounds and argued on such grounds before the state court.

Appellant in his Supplemental Brief, at page 3, quotes:

" 'Due process of law' contemplates a trial in a criminal case by a fair jury with full evidence and correct instructions as to the law. *Henderson v. State*, Fla., 20 So. 2d 659, (649), 661 (651)."

But on this point the Supreme Court of the United States has ruled to the contrary in *Buchalter v. New York* (1943), 319 U.S. 427, 63 S. Ct. 1129, 87 L. Ed. 1492, 1495-1496.



see also: *Davis v. State of Texas*, *supra*, 139 U.S. 651, 11 S. Ct. 675, 35 L. Ed. 300.

"*Due Process of Law*" by Taylor, *supra*, Section 551, p. 824.

Appellant states on page 3 of his Brief: "In criminal cases, 'due process of law' contemplates proper instructions on reasonable doubt." He cites *Howard v. Fleming*, 191 U.S. 126, 24 S. Ct. 49-51, 48 L. Ed. 121. On the contrary this case merely held that the "due process" clause of the Fourteenth Amendment was not violated by a failure of a state court to instruct a jury in a criminal case on the presumption of innocence.

Appellant also states on page 3 of his Brief: "In criminal cases, 'due process of law' is denied by instructions which set at naught the established principles of reasonable doubt." He again cites *Howard v. Fleming*, 191 U.S. 126, 24 S. Ct. 49, 50, 51, 48 L. Ed. 121, and in addition thereto cites *Chaffee v. United States*, 85 U.S. 516, 545, 21 L. Ed. 909, 914, and *Paddock v. United States*, 79 F. (2d) 872, 877. These last two cases do not discuss the question of "due process" at all.

2. **ASSUMING ARGUENDO THAT A FEDERAL QUESTION IS INVOLVED HEREIN, THE WRIT OF ERROR SHOULD BE DISMISSED BECAUSE SUCH FEDERAL QUESTION IS NOT SUBSTANTIAL.**

On this point we wish to refer the Court not only to the cases cited on page 18 of Territory's Answering Brief but also to all the federal cases cited therein from pages 19 to 39, both inclusive.

In *Hopt v. Utah*, 120 U.S. 430, 439-441, 7 S. Ct. 614, 30 L. Ed. 708, the Supreme Court of the United States upheld an instruction on reasonable doubt which contained the words:

*"That a reasonable doubt is a doubt based on reason, and which is reasonable in view of all the evidence."* (Emphasis ours.)

3. **THE CIRCUIT COURT OF THE FIRST JUDICIAL CIRCUIT, TERRITORY OF HAWAII, DID NOT ERR IN GIVING TO THE JURY TERRITORY'S INSTRUCTION NO. 9, ON REASONABLE DOUBT.**

The instruction in controversy reads as follows and the portion in italics indicates the part involved in this appeal:

**"TERRITORY'S INSTRUCTION NO. 9**

I further instruct you that the burden of proof is upon the Territory and the law presumes the defendant to be innocent, and this presumption continues and attends him at every stage of the case until it has been overcome by evidence which proves him guilty to your satisfaction and beyond a reasonable doubt. And in this connection, I instruct you that the doubt which will entitle the

defendant to an acquittal must be a reasonable doubt, not a conjured-up doubt, such a doubt as you might conjure up to acquit a friend, but a *doubt that you could give a reason for*.

A reasonable doubt is not a slight doubt, not a probable doubt, not a possible doubt, not a conjectural doubt, not an imaginary doubt, not a doubt of the absolute certainty of the guilt of the accused, because everything relating to human affairs and depending upon mortal evidence is open to conjectural or imaginary doubt, and because absolute certainty is not required by law. The real question is whether after hearing the evidence and from the evidence you have or have not an abiding belief, amounting to a moral certainty that the defendant is guilty and if you have such belief so formed, it is your duty to convict and if you have not such belief so formed it is your duty to acquit." (Record pp. 8-9.) (Emphasis ours.)

This Court, during the oral argument of its own motion, raised the question of the effect of the term "probable" used in the instruction.

This Court in *Hargreaves v. United States*, (CCA 9), 75 F (2d) 68, at page 73 states:

"It is a well-settled principle of law that in determining the correctness of instructions, detached phrases and sentences cannot be singled out and considered alone, but must be construed with their context." (citing authorities.)

See also: *Morrissey v. United States*, (CCA 9), 67 F (2d) 267, 273.

We have already shown in Territory's Answering Brief, pages 19-55, by the overwhelming weight of authority, both federal and state, including the decisions of this Court, that the term ". . . but a doubt you can give a reason for . . .," does not constitute error.

The appellant in his Supplemental Brief has not controverted this fact in any way but in effect claims that the use of the word "probable doubt" contained in the second paragraph of Instruction No. 9 may be a reasonable doubt and constitute a reversible error.

This again isolates a phrase of a single instruction without considering that phrase in relation to the balance of the instruction. The phrase as used in the instruction in controversy implies a "doubt" similar to a slight, possible or imaginary doubt and nothing else, and is intended to illustrate that absolute certainty of guilt can not be achieved and is not, therefore, required by law.

A fair reading and analysis of this instruction show in clear and unmistakable language that:

(1) The burden of proof is upon the Territory to prove the defendant guilty beyond a reasonable doubt.

(2) The defendant is presumed to be innocent until proven guilty beyond a reasonable doubt, and

(3) The definition of a reasonable doubt is according to the classical definition of Justice Shaw in *Commonwealth v. Webster*, 5 Cush. (Mass.) 295, at page 320. Thus, the term "probable doubt," considering the whole instruction could not in any way have misled or confused the jury.

In *People v. Lee Sare Bo*, 72 Cal. 623, 14 Pac. 310, the Supreme Court of California stated at page 312:

"3. In the charge to the jury the court, speaking on the subject of reasonable doubt, gave Mr. Chief Justice Shaw's definition thereof, which has been so often approved here, but, unfortunately, threw in this meaningless expression: '*But mere probabilities of innocence or doubts, however reasonable, which beset some minds on all occasions should not prevent such a verdict.*' What the court meant by mere probabilities of innocence or doubts which beset some minds on all occasions, in view of the correct and unambiguous language of the charge upon the same matter before and after this expression it is difficult to conjecture; but from the language following it would appear that the court desired to say to the jury that mere chimerical or fanciful doubts should not prevent a verdict if they were satisfied to a moral certainty of the guilt of the defendant. The court went on to say: 'In other words, gentlemen, a reasonable doubt, in a legal sense, is a doubt which has some reason for its basis; it is not a doubt arising from mere caprice or groundless conjecture, but it must arise from the facts proven in the case. You have no right to go outside of the evidence to hunt for doubts, nor



should you entertain those which are merely chimerical, or based on groundless conjectures.

It is that state of the case which, after an entire consideration and comparison of all the evidence, leaves your minds in that condition that you cannot say you feel an abiding conviction, to a moral certainty, of the truth of the charge. . . . The hypothesis contended for by the people must be established to an absolute certainty, to the entire exclusion of any rational probability of any other hypothesis being true, and, if a reasonable doubt is entertained by the jury on any material fact in the case, they should acquit.' The language of the sentence to which this objection is addressed is so ambiguous, and the charge in other portions so strong and clear on the question of reasonable doubt, we think the jury could not have been misled." (Emphasis ours.)

In 53 *American Jurisprudence, Trial, Section 842, p. 618*, we find the rule stated:

"Construction as a Whole.—In considering the correctness and adequacy of a charge to the jury, it should be taken as a whole and read in its entirety; that is, each instruction must be considered in connection with others of the series referring to the same subject and connected therewith, and if, when taken together, they properly express the law as applicable to the particular case, there is no just ground of complaint, even though an isolated and detached clause is in itself inaccurate, ambiguous, incomplete, or otherwise subject to criticism. The rule is applicable in both civil and criminal cases."

In *Peters v. United States*, (CCA 9), 94 F 127, 146, we find:



"The charge must be read and considered in its entirety; . . ."

In *Colt v. United States*, (CCA 8), 190 F 305, 308, the Court states:

"But the correctness of a charge is not to be determined upon excerpts taken therefrom, and considered apart from other portions bearing upon the same subject. The charge as a whole upon that question must be considered. So considered it cannot be successfully contended that the charge in question is erroneous."

This case was cited with approval in *Hargreaves v. United States*, (CCA 9), 75 F (2d) 68, 73.

Considering all the instructions on reasonable doubt given by the trial court in the case at bar the appellant was fully protected and the jury was not misled or confused by Territory's Instruction No. 9, either in the use of the phrase "a doubt that you could give a reason for" or the phrase "not a probable doubt."

The court, in addition to Territory's Instruction No. 9 gave the following instructions for appellants on reasonable doubt, to wit:

**"DEFENDANT'S INSTRUCTION NO. 2**

I instruct you that the issue which you are to try is that presented by the indictment, and the defendant's plea of not guilty in this case. For be it remembered that the plea of not guilty puts in issue and requires the *prosecution to prove each and every material allegation in the indictment beyond*

*all reasonable doubt.”* (Record p. 10.) (Emphasis ours.)

**“DEFENDANT’S INSTRUCTION NO. 3**

The indictment in this case is a mere accusation and is not of itself any evidence, not the slightest, of the defendant’s guilt, and no juror should permit himself to be to any extent influenced because or on account of the indictment against the defendant. *You are instructed that the defendant is presumed by the law to be innocent of the crime charged against him, in each and all its parts, and this presumption shields and protects him throughout each and every stage of the trial until overcome by satisfactory evidence, which convinces you of his guilt as charged beyond all reasonable doubt.”* (Record pp. 10-11.) (Emphasis ours.)

**“DEFENDANT’S INSTRUCTION NO. 4**

Moreover, I instruct you that this presumption of innocence is not a mere form to be disregarded by you at pleasure, but it is an essential, substantial part of the law of the land, and is binding upon you in this case, and it is your duty to give the defendant the full benefit of this presumption and to acquit him unless, as I have already stated, the evidence satisfies you of his guilt beyond all reasonable doubt.” (Record p. 11.)

**“DEFENDANT’S INSTRUCTION NO. 7**

Under the law no jury can convict a person charged with crime upon mere suspicion, however strong, or simply because there is a preponderance of all the evidence in the case against him, or simply because there are strong reasons to suspect him guilty. What the law requires before a person can

be convicted of crime is not suspicion, not mere probabilities, *but proof which excludes all reasonable doubt of his innocence.*" (Record p. 12.) (Emphasis ours.)

The cases cited by Appellant are not in point and the conclusion that a "reasonable doubt" justifying an acquittal in a criminal action may be a "probable doubt" does not follow.

Solicitude for defendant's rights is only one-half of the story. Solicitude for the rights of the Territory has equal consideration and weight, thus the question is not one of solicitude for either party but of determining in this particular case whether or not reversible errors has been committed.

The fact that *Griggs v. United States*, 158 F 572, was decided by this Court in 1908 and *Louie Ding v. United States*, 246 F 80, was decided in 1917 does not affect the positive rule of law enunciated in each case.

In the recent case of *Mansfield v. United States*, 76 F (2d) 224, 230, the United States Circuit Court of Appeals for the Eighth Circuit held in 1935 that an instruction on reasonable doubt which contained the words " a doubt for which you could give a reason" did not constitute error.

To the same effect, see *Murphy v. United States*, 33 F (2d) 896; Certiorari denied, 280 U.S. 584, 50 S. Ct. 35, 74 L. Ed. 634.

In *Hopt v. Utah*, 120 U.S. 430, 439-441, 7 S. Ct. 614, 30 L. Ed. 708, the Supreme Court of the United States upheld an instruction on reasonable doubt which contained the words "*that a reasonable doubt is a doubt based on reason*, and which is reasonable in view of all the evidence." (Emphasis ours.)

This is very similar to the words objected to in Territory's Instruction No. 9.

In *Marshall v. United States*, 197 F 511, 512-513, Certiorari denied, 226 U.S. 207, 33 S. Ct. 112, 57 L. Ed. 379, the Court held that an instruction on reasonable doubt did not constitute error which contained the following:

"—A doubt that you can give a reason for if the court called on you to give one."

### CONCLUSION

It is again respectfully submitted that the appellant has not shown that this Court has or should take jurisdiction of this case and that the trial court did not err in giving the jury Territory's Instruction No. 9 on reasonable doubt.

The error assigned is without merit and the judgment appealed from should be affirmed.

Dated at Honolulu, T. H., this 22nd day of November, A.D. 1946.

Respectfully submitted,

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Receipt of three copies of the foregoing brief is acknowledged this 22 day of November, A. D. 1946.

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